Office-Supreme Court, U.S.
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84-352
No. .....

IN THE

Supreme Court of the United States

OCTOBER TERM, 1984

JOHN CODY, ROBERT SASSO, JOHN DEE, WILLIAM ARGENTO, RALPH GUERCIA, HERBERT SCHNEIDER, and LOUIS NAPPI,

Petitioners,

VS.

RAYMOND J. DONOVAN, Secretary of the United States Department of Labor, and TED KATSAROS, JOHN KUEBLER, ROBERT TROTT, LAWRENCE KUDLA, and CHARLES CURD,

Respondents.

PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE SECOND CIRCUIT

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Questions Presented for Review

I. Whether the court of appeals contravened the Seventh Amendment to the United States Constitution and this Court's decision in *Beacon Theatres, Inc.* v. *Westover,* 359 U.S. 500 (1959), by affirming the district court's conduct of first severing "legal" third-party claims for which a jury trial had been demanded, from "equitable" main claims, and then conducting a bench trial of only the "equitable" claims without first trying the common factual issues between the "equitable" and "legal" claims before a jury.

II. Whether the unprecedented, excessive and unnecessarily punitive relief awarded by the district court, without ever hearing evidence relating to damages, and affirmed by the court of appeals, against the petitioner pension plan fiduciaries for making a single imprudent investment, including (1) damages in the full amount of the loss ostensibly suffered by the pension plan as a result of the imprudent investment, without considering any potential setoffs; (2) prejudgment interest at the above-prime rates that would have been realized by the imprudent investment; and (3) removal of the fiduciaries from their positions with not only the pension plan, but also its sister welfare, annuity and legal services trust funds, is justified under the Employee Retirement Income Security Act of 1974.

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PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE SECOND CIRCUIT

Petitioners John Cody, Robert Sasso, John Dee, William Argento, Ralph Guercia, Herbert Schneider and Louis Nappi respectfully petition this Court for a writ of certiorari to review the opinion and judgment of the United States Court of Appeals for the Second Circuit that was entered on June 29, 1984.

Opinions Below

The opinion of the court of appeals is not yet reported. The district court's July 21, 1983 opinion is reported as *Katsaros* v. *Cody*, 568 F. Supp. 360, 4 E.B.C. 1910 (E.D.N.Y. 1983). The district court's December 7, 1983 opinion is reported as *Katsaros* v. *Cody*, 4 E.B.C. 2613 (E.D.N.Y. 1983). The district court's January 26, 1984 opinion is reported

as *Katsaros* v. *Cody*, 4 E.B.C. 2698 (E.D.N.Y. 1984). The district court's April 5, 1983, April 15, 1983, August 18, 1983 and August 10, 1984 opinions are not reported.

Jurisdiction

The decision of the court of appeals was entered on June 29, 1984. (A.3a). The court of appeals denied a petition for rehearing on July 29, 1984. (A.2a). This petition was filed within ninety days after June 29, 1984. The jurisdiction of this Court is invoked under 28 U.S.C. § 1254(1).

Relevant Constitutional and Statutory Provisions

1. The Seventh Amendment to the United States Constitution provides:

> In suits at common law . . . the right of trial by jury shall be preserved . . . .

2. 29 U.S.C. § 1104 provides, in relevant part:

> Fiduciary duties
>
> (a)(1) Subject to sections 1103(c) and (d), 1342, and 1344 of this title, a fiduciary shall discharge his duties with respect to a plan solely in the interest of the participants and beneficiaries and—
>
> (A) for the exclusive purpose of:
>
> (i) providing benefits to participants and their beneficiaries; and
>
> (ii) defraying reasonable expenses of administering the plan;
>
> (B) with the care, skill, prudence, and diligence under the circumstances then prevailing that a prudent man acting in a like capacity and familiar with such matters would use in the conduct of an enterprise of a like character and with like aims;

(C) by diversifying the investments of the plan so as to minimize the risk of large losses, unless under the circumstances it is clearly prudent not to do so; and

(D) in accordance with the documents and instruments governing the plan insofar as such documents and instruments are consistent with the provisions of this subchapter.

3. 29 U.S.C. § 1105 provides, in relevant part:

Liability for breach of co-fiduciary

Circumstances giving rise to liability

(a) In addition to any liability which he may have under any other provision of this part, a fiduciary with respect to a plan shall be liable for a breach of fiduciary responsibility of another fiduciary with respect to the same plan in the following circumstances:

(1) if he participates knowingly in, or knowingly undertakes to conceal, an act or omission of such other fiduciary, knowing such act or omission is a breach;

(2) if, by his failure to comply with section 1104(a)(1) of this titl in the administration of his specific responsibilities which give rise to his status as a fiduciary, he had enabled such other fiduciary to commit a breach; or

(3) if he has knowledge of a breach by such other fiduciary, unless he makes reasonable efforts under the circumstances to remedy the breach.

4. 29 U.S.C. § 1109 provides, in relevant part:

Liability for breach of fiduciary duty

(a) Any person who is a fiduciary with respect to a plan who breaches any of the responsibilities, obli-

gations, or duties imposed upon fiduciaries by this subchapter shall be personally liable to make good to such plan any losses to the plan resulting from each such breach, and to restore to such plan any profits of such fiduciary which have been made through use of assets of the plan by the fiduciary, and shall be subject to such other equitable or remedial relief as the court may deem appropriate, including removal of such fiduciary.

Statement of the Case

Background

In February and March of 1979, petitioners, formerly the trustees of the Teamsters Local 282 Welfare, Pension, Annuity and Legal Services Trust Funds,[1] (the "Trustees") approved and disbursed a $2 million loan from the Pension Fund to the Des Plaines Bancorporation, Inc. (the "Bancorporation"), the corporate parent of the Des Plaines Bank (the "Bank"). In March 1981, when the principal balance due on the loan was $1.65 million, the Bancorporation defaulted in its repayment of the loan. Moreover, the Bank was closed by the FDIC and the Pension Fund was precluded from recovering against its principal collateral, a pledge of the outstanding stock of the Bank.

Following the Bancorporation's default, the respondents instituted their separate actions[2] against the Trustees al-

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[1] The Pension, Welfare, Annuity and Legal Services Funds are referred to collectively as the "Funds" and individually as the "Pension Fund," the "Welfare Fund," the "Annuity Fund" and the "Legal Services Fund."

[2] On July 14, 1981, respondents Katsaros, Kuebler, Trott, Kudla and Curd (the "Private Plaintiffs") brought an action in their capacities as participants in the Teamsters Local 282 Pension Trust Fund. *Katsaros* v. *Cody,* Civil Action No. 81-2277 (E.D. N.Y.). Subsequently, on July 1, 1982, respondent Raymond J. Donovan (the "Secretary") instituted a separate action in his

(footnote continued on following page)

leging that the loan was imprudent and constituted a violation by the Trustees of their fiduciary duties under Sections 404, 405 and 409 of the Employee Retirement Income Security Act of 1974 ("ERISA"), 29 U.S.C. §§ 1104, 1105 and 1109.

The Trustees subsequently commenced third-party actions in both the Private Plaintiffs' and the Secretary's actions seeking indemnity and contribution from the Bancorporation's and the Bank's directors, officers and counsel on the basis of their fraud and negligent misrepresentations in connection with the loan transaction. The Trustees demanded a trial by jury with respect to both third-party actions.

On April 5, 1983, the district court severed the Trustees' third-party actions from the main claims struck the Trustees' demands for jury trials of the main claims, consolidated the main claims for purposes of trial (A.30a-49a), and, shortly thereafter, denied the Trustees' application for reargument of, *inter alia*, the severance of the third-party actions. (A.50a-56a).

The district court conducted a consolidated three day bench trial only of the main ERISA claims on April 27-29, 1983. At the request of plaintiffs' counsel the district court bifurcated the trial and accepted evidence relating solely to the issue of the Trustees' liability. Thereafter, during the trial, the district court refused to allow the Trustees to introduce certain mitigating evidence by deeming it related to the issue of damages.

On July 18, 1983, ostensibly based on evidence adduced at trial, the district court found the Trustees liable for

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(footnote continued from preceding page)

capacity as Secretary of the United States Department of Labor. *Donovan* v. *Cody*, Civil Action No. 82-1920 (E.D.N.Y.).

Both cases were instituted in the United States District Court for the Eastern District of New York and assigned to Judge Jacob Mishler. By order of the district court dated April 5, 1983, they were consolidated for all purposes, including trial. (A.49a).

having breached their fiduciary duties under ERISA. (A. 57a-80a).

Five months later, in December 1983, without the benefit of any evidentiary proceedings regarding appropriate relief, the district court imposed damages against the Trustees, immediately removed and enjoined the Trustees from acting as fiduciaries of the Pension Fund, appointed independent asset and fund managers to manage the Pension Fund, and awarded costs and attorneys' fees to the plaintiffs. (A.98a-107a).

The district court subsequently entered as amended judgment, pursuant to applications by the plaintiffs, which joined the Welfare Fund, the Annuity Fund and the Legal Services Fund as defendants to both actions, removed and enjoined the Trustees from acting as fiduciaries of those Funds and extended the appointments of the asset and fund managers to include those Funds. (A.120a-124a).

On appeal, the court of appeals affirmed the findings and rulings of the district court in all material respects.[3] (A. 3a-27a).

Statements of Facts

By letter dated February 7, 1979, Jonathan T. Howe, in his capacity as counsel and a director of the Bancorporation and the Bank, contacted the fund manager of the Pension Fund and requested a loan from the Pension Fund to the Bancorporation in the amount of $2 million. In the letter, the Bancorporation proposed to repay the loan over four years with interest at the prime rate, and to pledge the Bancorporation's stock ownership of the Bank as security for the loan.

Subsequently, on February 27, 1979, Mr. Howe and Anthony G. Angelos, chairman of the board of directors

[3] The court of appeals did remand on the very narrow point that the district court had improperly enjoined the appointment of successor trustees for the Funds.

of the Bancorporation and the Bank and president of the Bank, appeared at a regularly scheduled Trustees' meeting at the Pension Fund's offices in E[illegible]ont, New York and made their formal application for the loan.

In connection with their presentation, Messrs. Howe and Angelos distributed certain financial statements reflecting the financial condition of the Bancorporation and the Bank, and of Mr. Angelos himself, and made certain representations to the Trustees regarding the need for the loan, the planned application of the loan proceeds, and the financial condition and viability of the Bancorporation and the Bank. Following the presentation and some preliminary negotiations, the Trustees agreed to send a committee of Pension Fund Trustees to Chicago the next day to continue negotiations for the loan.

The next day, two of the Trustees travelled to Chicago to continue negotiations for the loan. While in Chicago, the Trustees and their counsel met again with Messrs. Angelos and Howe and other officers, representatives and attorneys of the Bank and the Bancorporation. The representatives of the Bancorporation made additional representations to the Trustees during this period regarding the solvency and viability of both entities. Moreover, Jenner & Block, the counsel for the Bancorporation and the Bank, issued an opinion letter stating that neither entity was subject to any suits or proceedings which materially would effect its financial condition.

On March 1, 1979, following continuous discussions and negotiations, the two Trustees determined finally to allow the Fund to make the loan, and the transaction was closed.

The loan agreement provided for a $2 million loan by the Pension Fund to the Bancorporation, to be repaid over a four-year period, with interest at one percent above the prime rate, subject to a floor of ten percent. The Bancorporation was to repay the loan in semi-annual installments of $125,000 plus interest, with a final balloon payment of $1.25 million plus interest. The security for the

loan was 68,267 shares of capital stock of the Bank, representing approximately 95% of its outstanding shares. In addition, Mr. Angelos furnished his personal guarantee secured by second mortgages on two parcels of property of which he was part owner.

On March 1, 1981, two years after the loan was closed, the Bancorporation failed to make its semi-annual payment of principal and interest. Two weeks later, on March 14, 1981, the Bank was closed by the Federal Deposit Insurance Corporation (the "FDIC") and the Illinois Commissioner of Banks and Trust Companies, and placed under the receivership of the FDIC. The Bancorporation was not only unable to pay its remaining principal obligation of $1.625 million, but the principal collateral for the loan—the pledge of 95% of the Bank's stock—was rendered worthless.

The Trustees learned for the first time during discovery in connection with respondents' ERISA actions that, contrary to the representations made to them by the officers, directors and counsel for the Bank and the Bancorporation, the FDIC had issued a Confidential Report of Examination only several weeks before the loan was made. This Confidential Report of Examination concluded that the Bank was in dire financial straits and subject to being closed if certain corrective measures were not taken immediately. The Trustees initiated their third-party actions on the basis of that information, alleging violations of the federal securities laws[4] as well as common law fraud and negligent misrepresentations.

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[4] In its August 18, 1984 order, the district court dismissed the Trustees' federal securities law claims on the ground that the Pension Fund, not the Trustees, was the purchaser of securities, and therefore, the Trustees lacked standing to assert those claims. (A.90a-91a). The Trustees' common law claims remain pending, however, and on August 10, 1984, the district court ordered that they be transferred to the Northern District of Illinois. (A.133a).

REASONS FOR GRANTING THE WRIT

I.

The Decision of the Court of Appeals Upholding the Severance of the Trustees' Legal Claims From the Plaintiffs' Equitable Claims Is Contrary to This Court's Decision in *Beacon Theatres, Inc.* v. *Westover*, 359 U.S. 500 (1959), and Violates the Trustees' Right to Have a Trial by Jury of Their Legal Third-Party Claims.

The Trustees properly and timely demanded jury trials of their third-party actions against the Bancorporation officers, directors and attorneys (the "Bancorporation defendants"). These actions, which alleged violations of the federal securities laws as well as common law fraud and negligent misrepresentation, unquestionably were triable to a jury.[5] Nevertheless, before the trial of any claims, the district court severed the Trustees' third-party claims from the plaintiffs' ERISA claims and then conducted a bench trial only of the ERISA claims.[6]

By failing to resolve the factual issues common to the plaintiffs' "equitable" claims and the Trustees' "legal"

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[5] *See, e.g., Johns Hopkins University* v. *Hutton*, 343 F. Supp. 245, 249-50 (D. Md. 1972), *aff'd in part and rev'd in part on other grounds*, 488 F.2d 912 (4th Cir. 1973), *cert. denied*, 416 U.S. 916 (1974) (action under the Securities Act of 1933); *Aid Auto Stores, Inc.* v. *Cannon*, 525 F.2d 468, 469 n. 1 (2d Cir. 1975) (action under Securities Exchange Act of 1934); *Ford* v. *C.E. Wilson & Co.*, 30 F. Supp. 163 (D. Ct. 1939) (common law fraud action); and *Ransom* v. *Staso Milling Co.*, 2 F.R.D. 128, 131 (D. Vt. 1941) (negligence action). Nor is there any question that the Trustees' demand for a jury trial of these claims was timely and properly made.

[6] Although the Trustees demanded a trial by jury of the main ERISA claims as well, the district court struck that demand, finding, *inter alia*, that the ERISA claims were purely equitable in nature. (A.38a-39a). The court of appeals affirmed that ruling. (A.17a-18a).

third-party claims together, in a jury trial, the district court contravened the principles first set forth in *Beacon Theatres, Inc.* v. *Westover,* 359 U.S. 500 (1959), and effectively denied the Trustees' of their right to have a trial by jury.

On appeal, the court of appeals completely failed to consider whether the severance of the main and third-party claims violated the Trustees' Seventh Amendment right to have a jury trial of their third-party fraud claims. It found instead, citing Rule 42(b) of the Federal Rules of Civil Procedure, that the severance of the Trustees' third-party claims served the purposes of judicial economy and, therefore, was permissible. (A.16a). The court also denied, without explanation, the Trustees' petition for a rehearing with respect to this constitutional issue. (A.2a).

In *Beacon Theatres,* this Court ruled that where legal and equitable claims are presented in a single case and a trial by jury properly has been demanded with respect to the legal claims, the Seventh Amendment requires the factual issues common to the legal and equitable claims be tried to a jury:

> [Only] under the most imperative circumstances, circumstances which in view of the flexible procedures of the Federal Rules we cannot now anticipate, can the right to a jury trial of legal issues be lost through prior determination of equitable claims.

359 U.S. at 510-11 (footnote omitted), *cited with approval in Parklane Hosiery Co., Inc.* v. *Shore,* 439 U.S. 322, 351-52, 99 S. Ct. 645, 662 (1979) (footnote omitted) (Rehnquist, J. dissenting).

The major premise of the decision in *Beacon Theatres* was the recognition that prior equitable determination of issues common to both legal and equitable claims may work a collateral estoppel, foreclosing relitigation of the same issues before a jury. "To avoid this result, the [*Beacon*

Theatres] Court held that when legal and equitable claims are joined in the same action, the trial judge has only limited discretion in determining the sequence of trial and 'that discretion . . . must, wherever possible, be exercised to preserve jury trial.' *Id.* at 510, 79 S. Ct. at 956." *Parklane Hosiery Co., Inc.* v. *Shore,* 439 U.S. at 335, 99 S. Ct. at 653 (Stewart, J. for the Court).

The principles enunciated in *Beacon Theatres* and its progeny apply here to require a trial by jury of the Trustees' third-party claims. Although this Court has "recognized that an equitable determination can have collateral-estoppel effect in a *subsequent* legal action [without violating] the Seventh Amendment," *Parklane Hosiery Co., Inc.* v. *Shore,* 439 U.S. at 335, 99 S. Ct. at 653, *citing Katchen* v. *Landy,* 382 U.S. 323, 86 S. Ct. 467 (1966) (emphasis added), this case presents the much different situation where the equitable determination can have collateral estoppel effect in a *legal third-party action* initiated in connection with, and before trial of, the main equitable action.

Unquestionably, the Trustees' "legal" third-party claims and the plaintiffs' "equitable" ERISA claims were presented in the context of one lawsuit.[7] Indeed, the Trustees impleaded the Bancorporation defendants in the same ac-

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[7] In *Katchen* v. *Landy* this Court ruled that a bankruptcy court's prior equitable determination of a preference claim would not violate the Seventh Amendment even though the preference issue would be triable to a jury in a *subsequent plenary action.* 382 U.S. at 338, 86 S. Ct. at 470. Likewise, in *Parklane,* the Court ruled that a prior determination that defendants had violated the federal securities laws in an equitable declaratory judgment action brought by the SEC could, without violating the Seventh Amendment, bar relitigation of those same issues *in a subsequent private action for damages.* 439 U.S. at 333-37, 99 S. Ct. at 652-55.

Clearly the Trustees' third-party claims are akin more to the legal counterclaims presented in *Beacon Theatres,* which this Court found had to be tried to a jury before any equitable determination, and not to the subsequent actions that concerned this Court in *Parklane.*

tion and on the basis of the same transaction which premised the plaintiffs' ERISA claims.

Moreover, the claims of the Trustees and of the plaintiffs involved common legal and factual issues. The Trustees' third-party claims against the Bancorporation defendants were premised upon misrepresentations made during the negotiations for the Bancorporation loan. In order to prevail in those claims, the Trustees are required to prove, among other things, that they relied *justifiably* upon those misrepresentations. They also have to rebut the affirmative defense that their own lack of due diligence, if any, and not the third-party defendants' recklessness, was the prevailing cause of their loss.[8]

The ERISA actions focused upon whether the Trustees acted diligently in their investigation and review of the Bancorporation loan investment. After trying the plaintiffs' ERISA claims, the district court ruled that the Trustees had breached their fiduciary duties by failing adequately to investigate the veracity of these same representations.[9] (A.67a-77a). Effectively, therefore, the district court has already made findings of fact regarding the Trustees' conduct and diligence in connection with the loan transaction that are material and relevant to the

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[8] Although the Trustees' lack of due diligence should not be a defense to the third-party defendants' intentional fraud, *see, e.g., Sundstrand Corp.* v. *Sun Chemical Corp.*, 553 F.2d 1033, 1040 (7th Cir.), *cert. denied*, 434 U.S. 875 (1977); *Holdsworth* v. *Strong*, 545 F.2d 687 (10th Cir. 1976), *cert. denied*, 430 U.S. 955 (1977), it must be compared with the third-party defendants' negligent or reckless conduct for purposes of the Trustees' negligent misrepresentation claims. *Cf. Sundstrand Corp.* v. *Sun Chemical Corp.*, 553 F.2d at 1048 (plaintiff's due diligence is relevant when securities fraud defendant is to be liable for recklessness).

[9] Although the district court and the court of appeals apparently do not agree, the Trustees submit that the fact that they were defrauded in connection with the Bancorporation loan investment is a factor that should have been considered in any equitable or other proceeding to determine whether they acted imprudently.

third-party claims, and the court of appeals has affirmed those findings. (A.18a-20a).

As a result of the district court's prior factual determinations, the Trustees may be collaterally estopped from litigating their third-party claims before a jury. All of the requisite elements of collateral estoppel are present: the parties to be estopped—the Trustees—were parties to the earlier proceeding; the issues are the same as decided in the earlier proceeding; the issues were material to the earlier proceeding; and there has been a final determination in the earlier proceeding. *See, e.g., Haize* v. *Hanover Ins. Co.*, 536 F.2d 576, 579 (3rd Cir. 1976).

Indeed, the likelihood that the Trustees will be collaterally estopped from prosecuting their third-party claims is shown by the fact that the United States District Court for the Northern District of Illinois—*the court to which the Trustees' third-party claims have now been transferred* (A.133a-35a)—recently ruled in a related action that the Pension Fund, by virtue of its and the Trustees' litigation of the "justifiable reliance" issue in the Private Plaintiffs' and Secretary's actions, was collaterally estopped from relitigating that issue in its independent action for securities fraud, common law fraud and negligent misrepresentation against the Bancorporation defendants. *Teamsters Local 282 Pension Trust Fund* v. *Angelos*, Civil Action No. 84 C. 1312, slip. op. (N.D. Ill. June 8, 1984).[10] The district court, however, had all of these claims before it in the context of one action and chose,

[10] A copy of the Memorandum Opinion and Order of the United States District Court for the Northern District of Illinois is included in the appendix to this Petition. (A.125a-132a). Although the Pension Fund is appealing that ruling to the United States Court of Appeals for the Seventh Circuit, Docket No. 84-2141 (7th Cir.), the mere likelihood, much less the fact, that other courts would employ the ERISA court's ruling as a basis for collateral estoppel is enough to show that the Trustees' constitutional rights were at least improperly outweighed by considerations of judicial economy.

for its convenience and without regard for the Trustees' constitutional rights or this Court's mandate in *Beacon Theatres,* to sever the main and third-party claims and to try the main claims first without a jury. The court of appeals improperly affirmed that ruling.

Thus, in light of the clear impairment of the Trustees' constitutional rights and the authority of *Beacon Theatres,* this Court should grant the writ and decide this important Seventh Amendment question.

II.

The Relief Sanctioned by the Court of Appeals Is Absolutely Unprecedented, Unnecessarily and Unjustifiably Punitive, and Contrary to the Authority and Spirit of ERISA.

The relief awarded against the Trustees, which the court of appeals approved, was outrageously excessive and, therefore, cannot be permitted to stand.

The district court limited the trial of the ERISA action to the issue of the Trustees' liability and excluded all mitigating evidence. The district court then fashioned relief without holding a trial or any evidentiary hearing to determine the appropriate relief.

On appeal, the court of appeals held that the district court acted properly in bifurcating the trial into liability and damages phases since "the two phases involved different types of evidence." (A.17a). The court of appeals wholly failed to consider, however, that no trial or hearing as to appropriate relief was ever held.

Without considering that the Trustees were denied their opportunity to offer mitigating evidence the court of appeals sanctioned, *inter alia,* the imposition against the Trustees of joint and several liability in the amount of $2,530,064, which included the full amount of the loss

ostensibly suffered by the Pension Fund, without set-offs, and prejudgment interest at the "prime-plus-one-percent" interest rate provided in the Bancorporation loan documents; and the removal of the Trustees from the Pension Fund, the Annuity Fund, the Welfare Fund and the Legal Services Fund. Each aspect of the relief sanctioned by the court of appeals is excessive in its own right; when taken as a whole, the relief is outrageous and obviously punitive.

A. *Removal Is Not Justified for Mere Errors of Judgment.*

The court of appeals addressed the removal issue in one sentence of its opinion. After stating that removal under ERISA is appropriate where trustees have engaged in "repeated or substantial violations of their responsibilities," the court held that removal was justified "[s]ince the trustees here acted imprudently with respect to the Green loan[11] and the Bancorporation loan."

In its cursory analysis, the court of appeals failed fully to consider the seriousness of the breach of duty necessary to justify removal under ERISA. It also ignored the excessive nature of the ancillary relief it sanctioned.[12]

The court of appeals sanctioned removal of the Trustees based upon two isolated incidents of imprudence. Neither

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[11] In 1977, the district court enjoined the Pension Fund's proposed loan to Hyman Green on the ground that it violated ERISA's diversification requirements. *Marshall* v. *Teamsters Local 282 Pension Trust Fund*, 458 F. Supp. 986 (E.D.N.Y. 1977) (Mishler, J.). The facts relevant to that loan are set forth in the court of appeals' opinion. (A.3a-27a).

[12] The removal of the Trustees not only from the Pension Fund, but from the other Funds as well, is particularly disturbing. The Trustees never have been found to have breached their fiduciary duties with respect to the Welfare, Annuity and Legal Services Funds. Nor did the district ever obtain jurisdiction over those Funds. The district court simply deemed the plaintiffs' complaints amended to include those Funds as parties, and then removed the Trustees from their fiduciary positions. Accordingly, there is absolutely no basis for their removal from those Funds.

the Green loan nor the Bancorporation loan presented any allegation any more serious than that the Trustees had committed a mere error in their business judgment. The court of appeals had before it, therefore, only two incidents of investment imprudence by the trustees in over incidents of investment imprudence by the Trustees in over have never been accused of self-dealing, personally profiting or acting with divided loyalties; nor have they ever been found to have acted imprudently in connection with their management of the other Funds.

Trustee Guercia, moreover, was not even a trustee at the time of the Green loan. He cannot, therefore, be held responsible for any breaches of fiduciary duties occurring in that connection. *Cf.* ERISA § 409(b), 29 U.S.C. § 1109 (b) ("[n]o fiduciary shall be liable with respect to a breach of fiduciary duty . . . committed before he became a fiduciary"). Nevertheless, the court of appeals justified his removal solely on the extremely questionable basis that "it would be infeasible to allow him to maintain his position while removing the other trustees in favor of a court-appointed asset manager and fund manager." (A. 24a n.10). And yet, no provision was made for Trustee Guercia's reinstatement, even though the court of appeals itself obviated the basis for his removal by remanding and ordering that the court-appointed fund manager be replaced by successor trustees selected in accordance with the trust indenture. (A.24a-27a).

Although removal of breaching fiduciaries is expressly authorized by ERISA § 409(a), 29 U.S.C. § 1109(a), it is an extremely severe remedy which is entirely unjustified, inappropriate and unnecessary in this case where there are no allegations, much less evidence, of self-dealing or divided loyalties by the Trustees.

Because of the severity of the remedy, the courts traditionally have been reluctant to order removal of breach-

ing fiduciaries. "It is not every mistake or neglect of duty, in short, that requires or justifies removal." *Busby* v. *Worthen Bank & Trust Co., N.A.*, 484 F. Supp. 647, 653 (E.D. Ark. 1979); *cf.* 76 Am.Jur.2d *Trusts*, § 129 at 370 (because of the serious consequence of the remedy, "judicial removal or discharge of a trustee cannot be grounded in mere error of judgment or conduct even though the same is a technical breach of trust, at least where the trust estate . . . will be reimbursed").

The legislative history and case law development of ERISA reflects recognition and adoption of the common law's hesitancy to remove trustees, and they have authorized removal only "for repeated or substantial violation[s]." S. Rep. No. 383, 93rd Cong., 2d Sess., *reprinted in* 1974 U.S. Code Cong. & Ad. News 4890, 4989, *cited in Marshall* v. *Snyder*, 572 F.2d 894, 901 (2d Cir. 1978). Moreover, the case law makes clear that the "repeated and substantial" violations required to justify removal must be egregious and numerous.

In *Donovan* v. *Mazzola*, 716 F.2d 1226 (9th Cir. 1983), *cert. denied*, 104 S. Ct. 704 (1984), for example, "[t]he Pension Fund incurred substantial losses as a result of the below-market-interest-rate charged to the Convalescent Fund[, and] numerous other ERISA violations. . . ." *Id.* at 1238. Nevertheless, the court did not remove the pension fund trustees but permitted them to continue as fiduciaries subject to the control of an independent asset manager.

Marshall v. *Kelly*, 465 F. Supp. 341 (W.D. Okla. 1978) also illustrates the judicial reluctance to remove breaching fiduciaries. In *Kelly*, the defendant, the sole trustee and administrator of, and a participant in, a profit-sharing plan sponsored by his wholly-owned company, caused the plan to make excessive loans to his company and himself personally, on an uncollateralized basis and at below-normal interest rates. *Id.* at 345-47. In addition, he caused the

plan to sell its most lucrative asset at a bargain price at a time when the plan was in dire straits due to his other imprudent practices. He then personally profited from that sale by taking a six percent sales commission, and causing another one-third of the proceeds to be paid to his company as repayment of a fictitious construction loan. *Id.* at 347-49. Even though the court concluded that the defendant's breaches were "substantial and . . . *malum in se* rather than *malum prohibitum*," *id.* at 354, it merely precluded the defendant from resuming his fiduciary position until he repaid the plan for all outstanding loans to him and his company. *Id.*

When the Trustees' good faith conduct, which at most amounts to mere errors in judgment, is compared to the limited number of egregious cases where removal has been judicially sanctioned it is apparent that the court of appeals misconstrued the scope and nature of relief available under ERISA.

B. *The Prejudgment Interest Rate Is Unprecedented and Inequitable.*

The computation of prejudgment interest sanctioned by the court of appeals similarly is completely without legal support.[13]

The court of appeals approved of the district court's award of prejudgment interest at the "prime-plus-one-percent" interest rate, with its vague statement that "[a]warding prejudgment interest in accord with prevailing interest rates is consistent with prior case law." (A. 23a). The court of appeals however, misconstrued "prior

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[13] As previously noted, prejudgment interest was assessed at the "prime-plus-one-percent" interest rate provided for in the Bancorporation loan documents until the maturity date of the loan, and thereafter at the prevailing prime rate.

case law" in sanctioning this excessive award of prejudgment interest.[14]

Although, as the court of appeals noted (A.22a-23a), an assessment of prejudgment interest is discretionary with the trial court, that discretion must be "equitably exercised in light of the character of the breach and the degree of fault." *Gilliam* v. *Edwards,* 492 F. Supp. 1255, 1267 (D. N.J. 1980). Moreover, an assessment of prejudgment interest must begin by reference to the general rule that "where a trustee is chargeable with interest, he is chargeable with simple interest at the legal rate." *Donovan* v. *Bryans,* 566 F. Supp. 1258, 1265 (E.D. Pa. 1983).

The court of appeals, in sanctioning the prejudgment interest award, failed to take into account the "character" of the Trustees' ostensible imprudence and their degree of fault in causing loss to the Pension Fund. When these factors are considered and measured against misconduct of other trustees found to justify only simple interest at the legal rate, it is clear that the prejudgment interest award is unjustified and excessive.

In *Brink* v. *DaLesio,* 667 F.2d 420 (4th Cir. 1981), for example, the defendant fiduciaries were found to have engaged in a surreptitious arrangement of self-dealing whereby they personally and improperly profited from the use of fund assets. *Id.* at 423. Likewise, in *Bryans,* the defendant fiduciaries admittedly made loans to themselves

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[14] Indeed, the two cases cited by the court of appeals to justify an award of interest at the prime-plus-one-percent rate are entirely inapposite.

The court in *Donovan* v. *Mazzola,* 716 F.2d 1226 (9th Cir. 1983), *cert. denied,* 104 S. Ct. 704 (1984), made no specific determination as to an award of interest, but merely found that the plan trustees had breached their fiduciary duties by lending money at below the market rate.

In *Freund* v. *Marshall & Isley Bank,* 485 F. Supp. 629 (W.D. Wis. 1979), the court awarded prejudgment interest at the prime rate, but only after finding that that rate was "the minimum rate which the plan was earning on its investments." *Id.* at 644.

and their businesses from their fund which they did not intend to repay. 566 F. Supp. at 1266. Nevertheless, the courts in both cases assessed only simple interest at the legal rate.

Unlike the defendants in *Brink* and *Bryans,* the Trustees have not engaged in any self-dealing, nor have they personally profited from their allegedly imprudent investments. Indeed, all of their investments have been made for the sole purpose of earning a profit for the Pension Fund, the best evidence of which is the extremely appealing interest rate negotiated in connection with the Bancorporation loan.

The Trustees' "degree of fault" for the loss caused also militates against imposition of this unprecedented prejudgment interest rate. Intervening with and superseding the Trustees' determination to make the loan to the Bancorporation were the fraudulent representations of Messrs. Howe and Angelos and other Bancorporation representatives during negotiation of the loan, and the FDIC's unilateral, unannounced and practically unprecedented closing of the Bank which predicated the Bancorporation's default. Indeed, up until the time of the FDIC's closing of the Bank, the Bancorporation had regularly met its debt service obligations. Thus, if anyone is to blame for the Pension Fund's loss, that blame clearly cannot rest with the Trustees alone.

In sum, the Trustees acted with respect to the Bancorporation loan in good faith; even if they did act imprudently, any breach of their duties to the Pension Fund surely cannot be considered "egregious." Accordingly, the excessive prejudgment interest award, which so departs from prior precedent as to seem punitive in nature, cannot stand.

In *Donovan* v. *Bierwirth,* CV 81-3408, slip op. at 39 (E.D.N.Y. June 3, 1983) (Mishler, J.), the same district

court that presided over this action set forth a wholly different standard for computing interest in ERISA cases.[15]

In *Bierwirth*, the court held that damages for liability under ERISA § 404(a) are computed by adding "(1) the loss to the Plan, as alleged by the Secretary, at whatever fair value is ultimately found . . . plus (2) the income that the Plan would have earned if the funds used to purchase such securities were invested with other Plan assets." *Id.* at 13. In other words, the appropriate rate of interest, acording to the district court, is the average rate of return earned by the plan's other investments from the time of the breach. *See also Freund* v. *Marshall & Isley Bank*, 485 F. Supp. 629 (W.D. Wis. 1979) (court awarded interest at the minimum rate that the plan was earning on its investment); *Marshall* v. *Kelly*, 465 F. Supp. 341 (W.D. Okla. 1978) (court ordered money repaid at 10% interest which corresponded roughly to interest rates the plan earned on other investments). In this case, however, the district court was allowed to depart from its own standard for assessing prejudgment interest.

The testimony and exhibits introduced at trial, which were part of the record before the court of appeals, show that from the time of the Bancorporation loan, the Pension Fund's average annual rate of return was approximately 8 to 9 percent. The evidence also shows that the Bancorporation loan provided a rate of return unequalled by any of the Pension Fund's other investments. Nonetheless, by failing to consider the appropriate factors in assessing interest, the court of appeals sanctioned interest at rates as high as 18 and 19 percent which clearly are not justified by prior case law.[16]

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[15] *See Donovan* v. *Bierwirth*, 538 F. Supp. 463 (E.D.N.Y. 1981), *modified*, 680 F.2d 263 (2d Cir.), *cert. denied*, 103 S. Ct. 488 (1982).

[16] Indeed, it is obviously inequitable for a court to rule that an investment should never have been made, but then to require that restitution be made at the same terms as would have been afforded by the investment.

C. *The Failure to Consider Set-Offs Is Prejudicial to the Trustees.*

In December 1983, when it entered its judgment against the Trustees, the district court had been advised that the Pension Fund had made substantial recoveries through sales of the collateral for the Bancorporation loan. Had the district court properly taken evidence relating to damages, it would have known that the Trustees were entitled to a set-off of approximately $1 million. Instead, without hearing any evidence relating to the damages issue, the district court simply ordered that a final judgment be entered against the Trustees for the full amount due on the loan at the time of the Bancorporation's default and that "[p]ayments received by the [Pension] Fund on account of the loan will be credited against the judgment sum." (A.101a).

In response to the Trustees' argument that they are entitled to have their liability reflected in one comprehensive judgment, the court of appeals affirmed the district court's judgment, stating that the Trustees' "contention is answered by the district court's express provision" regarding credits against the judgment. (A.24a). This response, however, begs the question. The fact is that the Trustees are unnecessarily stigmatized with a $2.5 million dollar judgment against them, and with the burden of demonstrating in some subsequent proceeding that they are entitled to pre-judgment set-offs. Had the district court been required to do its own work, this stigma would not exist.

D. *The Totality of the Relief Is Outrageously Excessive and Obviously Punitive.*

When all of the aspects of the district court's relief are considered as a whole, it becomes obvious that the purpose of the relief was not to protect the Pension Fund but, instead, to punish the Trustees. The district court went out of its way to limit the issues before it, and, after

finding the Trustees liable for breaching their fiduciary duties, it imposed the harshest remedies available under the circumstances.

By affirming this relief in an ERISA action, the court of appeals has opened the door for punitive damages in an area where Congress arguably has refused to allow them. *Cf. Dependahl* v. *Falstaff Brewing Corp.*, 653 F.2d 1208, 1216 (8th Cir.), *cert. denied*, 102 S. Ct. 641 (1981) (court was persuaded that ERISA's silence with respect to punitive damages indicates Congressional intent that they not be recoverable); *accord Diano* v. *Central States, Southeast and Southwest Areas Health and Welfare and Pension Funds*, 551 F. Supp. 861 (N.D. Ohio 1982); *Hoskins* v. *Retirement Plan of Standard Oil Co.*, Civil Action No. 78-C3670, slip op. (N.D. Ill. Jan. 17, 1982); *see also Hammond* v. *James W. Griffin Co.*, 520 F. Supp. 162, 168 (N.D. Ga. 1971) (court refused to award both interest and liquidated damages stating that such a recovery "would constitute a penalty to defendants not sanctioned by . . . statute").

The court of appeals, by misconstruing prior judicial precedent and failing to take account of matters properly before it, sanctioned relief against the Trustees which is clearly excessive and without legal or equitable basis. Because of the obviously excessive nature of this relief, this Court should grant the writ, and decide this very important issue regarding the extent of relief available for breaches of fiduciary duties under ERISA.

CONCLUSION

For the foregoing reasons, the writ of certiorari should be granted.

Dated: New York, New York
September 4, 1984

Respectfully submitted,

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APPENDIX

Order of United States Court of Appeals

UNITED STATES COURT OF APPEALS
SECOND CIRCUIT

At a stated term of the United States Court of Appeals, in and for the Second Circuit, held at the United States Courthouse, in the City of New York on the 26th day of July one thousand nine hundred and eighty-four.

No. 83-6375

TED KATSAROS, JOHN KUEBLER, ROBERT TROTT, LAWRENCE KUDLA, and CHARLES CURD, as participants in the Teamsters Local 282 Pension Trust Fund,

Plaintiffs-Appellees,

v.

JOHN CODY, ROBERT SASSO, JOHN DEE, WILLIAM ARGENTO, RALPH GUERCIA, HERBERT SCHNEIDER and LOUIS NAPPI, as Trustees of the Teamsters Local 282 Pension Trust Fund,

Defendants-Appellants,

ANTHONY G. ANGELOS, C.J. BASSLER, JR., JONATHAN T. HOWE, CLARENCE L. JENSEN, LAMBROSE KARKAZIS, JAMES C. KIRIE, JAMES KOKONAS, and JAMES VERROS,

Third Party-Defendants,

LOCAL 282 INTERNATIONAL BROTHERHOOD OF TEAMSTERS, CHAUFFERS, WAREHOUSEMAN AND HELPERS OF AMERICA, MICHAEL CARBONE, MICHAEL BOURGAL, JOSEPH MATTARAZZO and EDWARD SILVERA,

Intervenors.

Order of United States Court of Appeals

RAYMOND J. DONOVAN, Secretary of United States Department of Labor,

Plaintiff-Appellee,

v.

JOHN CODY, WILLIAM ARGENTO, JOHN DEE, RALPH GUERCIA, LOUIS G. NAPPI, ROBERT SASSO, and HERBERT SCHNEIDER, and the TEAMSTERS LOCAL 282 PENSION TRUST FUND,

Defendants,

JOHN CODY, WILLIAM ARGENTO, JOHN DEE, RALPH GUERCIA, LOUIS G. NAPPI, ROBERT SASSO, and HERBERT SCHNEIDER,

Defendants-Appellants,

JOHN CODY, WILLIAM ARGENTO, JOHN DEE, RALPH GUERCIA, LOUIS G. NAPPI, ROBERT SASSO, and HERBERT SCHNEIDER,

Third Party Plaintiffs-Appellants,

v.

ANTHONY G. ANGELOS, C.J. BASSLER, JR., JONATHAN T. HOWE, CLARENCE L. JENSEN, LAMBROSE KARKAZIS, JAMES C. KIRIE, JAMES KOKONAS, ANTON A. SMIGIEL, JAMES VERROS and HERBERT C. WENSKE,

Third Party Defendants.

A petition for a rehearing having been filed herein by counsel for the defendants-appellants, John Cody, Robert Sasso, John Dee, William Argento, Ralph Guercia, Herbert Schneider and Louis Nappi, as Trustees of the Teamsters Local 282 Pension Trust Fund,

Upon consideration thereof, it is

Ordered that said petition be and it hereby is DENIED.

ELAINE B. GOLDSMITH
Clerk

Opinion of United States Court of Appeals

UNITED STATES COURT OF APPEALS
FOR THE SECOND CIRCUIT

No. 1065—August Term, 1983

Argued: May 3, 1984 Decided: June 29, 1984

Docket No. 83-6375

TED KATSAROS, JOHN KUEBLER, ROBERT TROTT, LAWRENCE KUDLA, and CHARLES CURD, as participants in the Teamsters Local 282 Pension Trust Fund,

Plaintiffs-Appellees,

—against—

JOHN CODY, ROBERT SASSO, JOHN DEE, WILLIAM ARGENTO, RALPH GUERCIA, HERBERT SCHNEIDER and LOUIS NAPPI, as Trustees of the Teamsters Local 282 Pension Trust Fund,

Defendants-Appellants,

ANTHONY G. ANGELOS, C.J. BASSLER, JR., JONATHAN T. HOWE, CLARENCE L. JENSEN, LAMBROSE KARKAZIS, JAMES C. KIRIE, JAMES KOKONAS, and JAMES VERROS,

Third Party Defendants,

LOCAL 282 INTERNATIONAL BROTHERHOOD OF TEAMSTERS, CHAUFFERS, WAREHOUSEMAN AND HELPERS OF AMERICA, MICHAEL CARBONE, MICHAEL BOURGAL, JOSEPH MATTARAZZO and EDWARD SILVERA,

Intervenors.

RAYMOND J. DONOVAN, Secretary of United States Department of Labor,

Plaintiff-Appellee,

—against—

Opinion of United States Court of Appeals

JOHN CODY, WILLIAM ARGENTO, JOHN DEE, RALPH GUERCIA, LOUIS G. NAPPI, ROBERT SASSO, and HERBERT SCHNEIDER, and the TEAMSTERS LOCAL 282 PENSION TRUST FUND,

Defendants,

JOHN CODY, WILLIAM ARGENTO, JOHN DEE, RALPH GUERCIA, LOUIS G. NAPPI, ROBERT SASSO, and HERBERT SCHNEIDER,

Defendants-Appellants,

JOHN CODY, WILLIAM ARGENTO, JOHN DEE, RALPH GUERCIA, LOUIS G. NAPPI, ROBERT SASSO, and HERBERT SCHNEIDER,

Third Party Plaintiffs-Appellants,

—against—

ANTHONY G. ANGELOS, C.J. BASSLER, JR., JONATHAN T. HOWE, CLARENCE L. JENSEN, LAMBROSE KARKAZIS, JAMES C. KIRIE, JAMES KOKONAS, ANTON A. SMIGIEL, JAMES VERROS and HERBERT C. WENSKE,

Third Party Defendants.

Before:

LUMBARD, MANSFIELD and KEARSE,

Circuit Judges.

Appeal from orders and judgments entered in the Eastern District of New York, Jacob Mishler, *Judge,* finding the appellants jointly and severally liable for losses incurred on account of breaches of their fiduciary duties under the Employee Retirement Income Security Act of 1974, 29 U.S.C. §§1001, *et seq.,* and removing the appellants as trustees of four union trust funds in favor of a court-appointed fund manager and an asset manager.

Affirmed in part and remanded in part.

EDWARD J. BOYLE, Esq., New York, NY (Thomas R. Manisero, Esq., Wilson, Elser, Edelman & Dicker, New York, NY, of counsel), *for Appellants Cody, Sasso, Dee, Argento, Guercia, Schneider and Nappi.*

ARTHUR Z. SCHWARTZ, Esq., New York, NY (Daniel E. Clifton, Esq., Susan M. Jennik, Esq., Joseph E. Gubbay, Esq., Hall, Clifton & Schwartz, New York, NY, of counsel), *for Appellees Katsaros, Kuebler, Trott, Kudla, and Curd.*

RICHARD P. CARR, Attorney, U.S. Department of Labor, Washington, DC (Francis X. Lilly, Solicitor of Labor, Robert N. Eccles, Acting Associate Solicitor, Plan Benefits Security Division, Norman P. Goldberg, Counsel for Fiduciary Litigation, Plan Benefits Security Division, U.S. Department of Labor, Washington, DC, of counsel), *for Secretary of Labor.*

ALEXANDER A. MIUCCIO, Esq., New York, NY (Robert F. Meehan, Esq., Altieri, Kushner & Miuccio, New York, NY, of counsel), *for Intervenor Association of New York City Concrete Producers, Inc.*

J. WARREN MANGAN, Esq., Long Island City, NY (O'Connor & Mangan, P.C., of counsel), *for Intervenor Local 282 I.B.T.*

ROBERT M. BAPTISTE, Esq. and DAVID J. GZESH, Esq., Washington, DC, *for Amicus Curiae International Brotherhood of*

Teamsters, Chauffers, Warehousemen and Helpers of America.

SHEA & GOULD, New York, NY (Peter D. Stergios, Esq., Alice P. Henkin, Esq., New York, NY, of counsel), *for Amicus Curiae The General Contractors Association of New York, Inc.*

MANSFIELD, *Circuit Judge:*

Appellant trustees[1] of the Teamsters Local 282 Pension Trust Fund, Welfare Trust Fund, Annuity Trust Fund, and Legal Services Trust Fund appeal from various judgments and orders[2] entered in the Eastern District of New York after a bench trial by Judge Mishler finding them jointly and severally liable for losses incurred by the Local

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[1] The trustees are John Cody, Robert Sasso, John Dee, William Argento, Ralph Guercia, Herbert Schneider, and Louis Nappi.

[2] The orders and judgments appealed from are:

(1) April 5, 1983 order striking appellants' demand for a jury trial, severing the appellants' third party actions from the main claims, and consolidating the main claims;

(2) April 22, 1983 order denying appellants' application for reargument of the denial of a jury trial and severance of the third party actions and appellants' motion for Judge Mishler's recusal;

(3) July 21, 1983 order finding the appellants liable for breaches of fiduciary duties on account of the Hyman Green loan and the Bancorporation loan;

(4) December 7, 1983 order and judgment mandating that the trustees reimburse the Pension Fund for losses incurred on account of the two loans and providing for the appointment of a fund manager and an asset manager to manage the Pension Fund until March 31, 1985; and

(5) December 27, 1983 order which joined the Welfare, Annuity, and Legal Services Funds as defendants in both actions, enjoined the trustees from acting as fiduciaries of those funds and extended the appointments of the asset and fund managers to include those funds.

282 Pension Trust Fund ("Pension Fund") on account of breaches of their fiduciaries duties under the Employee Retirement Income Security Act of 1974 ("ERISA"), 29 U.S.C. §§1001, *et seq.*, and removing them from their positions as trustees of four funds in favor of a fund manager and an asset manager appointed by the court to serve until March 31, 1985.

This appeal arises out of two separate actions consolidated by the district court, one of which was filed by a group of participants in the Pension Fund ("the private plaintiffs") and the other by the United States Secretary of Labor ("the Secretary"). Both actions alleged that the appellant trustees violated their fiduciary duty under ERISA when they made a $2 million loan in 1979 to Des Plaines Bancorporation, Inc. ("Bancorporation"). The private plaintiffs' action also alleged that the trustees violated their fiduciary duty under ERISA when they failed to collect $23,474 plus interest from one Hyman Green in connection with an aborted loan to Green in 1978. Appellants, joined in part by two intervenors—the Association of the New York City Concrete Producers, Inc. and Local 282 of the International Brotherhood of Teamsters[3] —argue that the court below erred in the following respects:

(1) in finding that the trustees violated their fiduciary duty under ERISA with respect to the Bancorporation loan and the Hyman Green loan;

(2) in finding them jointly and severally liable for all losses incurred on account of those loans;

(3) in removing them as trustees of the four funds in favor of a court appointed asset manager and fund manager authorized to serve until March 31, 1985;

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[3] The intervenor Association of New York City Concrete Producers challenges only the appointment of the receiver to serve until March 31, 1985, and the intervenor Local 282 challenges the removal of the trustees from their positions as well as the duration of the receiver's appointment.

(4) in denying their request for a jury trial;

(5) in severing the third-party claims asserted by appellants against others;

(6) in bifurcating the trial into liability and damages phases; and

(7) in Judge Mishler's refusal to recuse himself.

We affirm the orders of the district court with the exception of the appointment of the fund manager to oversee the operation of the fund until March 31, 1985. We conclude that the fund manager should perform his duties only until the union and the employers' association have chosen successor trustees who are acceptable to the court.

In February 1978, at a time when the assets of the Pension Fund were approximately $58 million, the trustees of that fund approved a $35 million loan to Hyman Green, $20 million of which was to be used to purchase 10 acres of land and construct a hotel and gambling casino on the "Strip" in Las Vegas, Nevada, and $15 million of which was to be used to purchase certain property from the Pension Fund in Southhampton, New York. As part of the loan agreement, Green expressly assumed responsibility for the Pension Fund's expenses in arranging the loan transaction. In April 1978, the United States Secretary of Labor commenced an action seeking to enjoin the Pension Fund and the trustees from making the loan to Green. In August 1978 Judge Mishler issued an order and judgment finding that the proposed loan violated the investment diversification and "prudent man" sections of ERISA, 29 U.S.C. §2204(a)(1)(B) and (C).[4] *Marshall* v. *Teamsters*

[4] The statute provides in relevant part:

"(a)(1) . . . a fiduciary shall discharge his duties with respect to a plan solely in the interest of the participants and beneficiaries and—

* * * * *

Local 282 Pension Fund, 458 F. Supp. 986 (E.D.N.Y. 1978). He enjoined the Pension Fund and the trustees from loaning the Fund's assets to Green and ordered the trustees to indemnify the Fund for any losses the Fund suffered as a result of the loan.

In November 1980 Green sued the Fund. The Fund counterclaimed for the $23,474 in expenses incurred by it in arranging the loan which had not been reimbursed by Green. Green's claim and the counterclaim are presently pending before Judge Mishler. The private plaintiffs then commenced this action in July 1981 seeking the $23,474 in unreimbursed expenses plus interest incurred in connection with the Green loan.

In the meantime, in January 1979, five months after Judge Mishler had enjoined the Fund's loan to Green, Anthony G. Angelos, president and chairman of the board of Bancorporation, informed John Cody, the Administrator of the Pension, Welfare, and Annuity Funds, that Bancorporation was seeking a loan by March 1, 1979, for its wholly owned subsidiary, the Des Plaines Bank ("the Bank"). On February 7, 1979, Jonathan T. Howe, a director and counsel to Bancorporation and counsel to the Bank, at Cody's suggestion wrote to Cody applying for a $2 million loan from the Fund to the Bank. Cody arranged for Howe to meet with the Fund's trustees at their February 27, 1979 meeting, which was the first time any of the trustees other than Cody learned of the proposed loan. At the meeting Howe distributed various financial statements of Bancorporation and the Bank: the consolidated

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"(B) with the care, skill, prudence, and diligence under the circumstances then prevailing that a prudent man acting in a like capacity and familiar with such matters would use in the conduct of an enterprise of a like character and with like aims;

"(C) by diversifying the investments of the plan so as to minimize the risk of large losses, unless under the circumstances it is clearly prudent not to do so; . . ."

financial statements of Bancorporation and the Bank as of December 31, 1978, the financial statement of the Bank as of December 31, 1978, and a comparative schedule of assets of the Bank as of December 31, 1977, November 30, 1978, and December 31, 1978. The three documents consisted of about 35 pages of figures and explanatory notes. Howe and Angelos made a two-hour presentation to the trustees and their certified public accountant, Harvey Colton, touching "on the highlights of the statement."

At trial Colton testified that neither he nor anyone on the Fund's staff had sufficient training to express an opinion as to the soundness of the loan. None of the trustees had an accounting or banking background. They were wholly unequipped personally to analyze the figures presented to them to find out whether any serious financial problems were faced by the prospective borrower. They lacked any expertise in such important matters as capital adequacy, quality of assets, liquidity, the value of the bank's stock, and the like. In short, they passively received a rosy superficial picture of the bank and its holding company from persons with an interest in obtaining their approval. No effort was made to obtain independent professional assistance or analysis of the financial data presented to them.

After some discussion the trustees voted to approve the $2 million loan to the Bancorporation subject to further review and negotiations in Chicago, the home of Bancorporation and of the Bank. The trustees appointed Cody and Ralph Guercia as a committee to examine the proposed security, to negotiate additional protective terms and, if matters proved satisfactory, to consummate the loan transaction. Cody and Guercia traveled to Chicago the next day, February 28, 1979, and continued discussions with Angelos and Howe. The two trustees visited the premises of the Bank and viewed the real estate that was to secure Angelos' personal guarantee of the loan. On the

following day, March 1, 1979, Cody and Guercia signed various loan documents on behalf of the Pension Fund and $2 million was disbursed as a loan by the Fund to the Bank. At their next meeting, which was on March 20, 1979, the trustees, including Louis Nappi, who had been absent from the previous meeting, voted to approve and ratify the loan to the Bancorporation.

The agreement provided for a $2 million loan by the Fund to Bancorporation, to be repaid over a four-year period. Interest was to be payable at prime plus 1%, with a 10% floor on the interest rate. Bancorporation was to repay the loan in semi-annual installments of $125,000 plus interest. At the end of four years, a final balloon payment of $1.125 million was to be made. The security for the loan was 68,267 shares of capital stock of the Bank, representing 95% of its outstanding shares. If the book value of the stock should go below $2 million, the Bank or Bancorporation would be required to put up additional collateral. In addition to the stock, Angelos furnished as security for the loan his personal guarantee secured by a second mortgage on two parcels of property owned in part (58% and 64% respectively) by Angelos. The loan agreement also required Bancorporation to submit financial statements to the Pension Fund on a regular basis.

The Pension Fund received bi-annual payments from Bancorporation, as required by the loan agreement, in a timely fashion in September 1979, March 1980, and September 1980. On March 14, 1981, however, the Bank was closed by federal and state regulatory officials. At that time, the Bancorporation owed the Pension Fund a total of $1.625 million plus interest from September 1, 1980. Bancorporation has made no further payments of interest or principal to the Fund.

At trial the Secretary's expert, John Duffy, who had prepared a report on the subject of the financial advisability of making the loan, testified concerning the financial

condition, performance, and credit-worthiness of the Bank (Bancorporation's sole asset) as of the time of the loan. Duffy concluded that there was ample information available to the trustees in February 1979 that pointed to the Bank's prospective failure. Neither the Bank nor Bancorporation had ever earned the amount of money needed to service the debt and there was nothing in the financial statements to suggest that they would be able to achieve such earnings in the future. The Bank's equity/asset ratio —3.46%—placed it 149th out of 151 Illinois banks in terms of that ratio, a fact which, according to Duffy, should have raised serious concerns "about how the loan would be repaid." Moreover, the tangible net worth of Bancorporation was only $500,000, after a $1 million "goodwill" entry on the balance sheet was subtracted. Duffy also observed that the abnormal rise in the amount of the Bank's loans (from $21 to $32 million between 1977 and 1978) should have prompted the trustees to "interrogate . . . management" as to the kind of loans being made and their actual value versus their book value.

Other testimony revealed that similar red flags would have been uncovered if a reasonably careful inquiry had been made. First, six days before the trustees' February 27, 1979, meeting, officials of the Federal Deposit Insurance Corporation ("FDIC") had met with the Bank's board of directors, urging the latter to adopt a corrective plan to deal with the bank's undercapitalization, poor loan-to-deposit ratio, insufficient liqiuidity, high percentage of risky loans, and improper lending practices. Second, Bancorporation owed its principal creditor, Central National Bank in Chicago, approximately $1 million, due March 1, 1979. Inquiry by the Fund would have revealed that Central National, to which 50% of the amount loaned was to be paid immediately, had refused for the third time to extend the Bancorporation loan and had advised Des Plaines

that if payment were not made in a timely fashion Central National would foreclose and take over the Bank. Moreover, at least five Chicago-area banks had refused to lend money to Bancorporation to refinance its debt to Central National Bank. Finally, the Fund's trustees failed to do more than have Cody and Guercia simply visit the property securing the Angelos guarantee. Further investigation would have revealed that on the day the loan agreement was signed (March 1, 1979) one of the two real estate parcels put up by Angelos as security for the loan was seized and sold for tax delinquencies. Moreover, both parcels turned out to be worth about a third of what Angelos had said they were worth.

The Fund's negligence with respect to the Bancorporation loan continued with the administration of the loan after it was disbursed. Although the Fund was entitled to regular financial statements from Bancorporation, it received only sporadic, incomplete financial information until the time of the bank's closing in March 1981. Even this information went largely unexamined. The trustees, Pension Fund staff, and the Fund's outside accountant never analyzed or reported upon the incomplete financial information that was furnished. The trustees also failed to exercise their right, set forth in the loan agreement, to demand additional, supplemental collateral equal to the $2 million loan amount. Finally, the trustees undercharged Bancorporation for interest amounts due on the loan for the period 1979 to 1980. Rather than apply the prime-plus-1% interest rate on a floating basis, as provided in the loan agreement, the trustees instead used the prime rate figure in effect 30 days before interest payments were due. As a result, the Fund received $32,500 less interest than it was entitled to during the course of the loan.

The actions filed by the private plaintiffs and the Secretary in July 1981 and July 1982, respectively, both alleged that appellants had breached their fiduciary duty as

trustees to the Pension Fund in making the loan to Bancorporation. The private plaintiffs also challenged the appellants' behavior with respect to recovering the expenses incurred in making the Green loan. The trustees answered both complaints and requested a jury trial with respect to the Secretary's action but not with respect to the action brought by the private plaintiffs. In November 1982 the trustees filed a third-party action against Bancorporation's directors and counsel, alleging fraud in connection with the loan transaction. The trustees demanded a jury trial in this third-party fraud action. In December 1982 the district court consolidated the actions by the Secretary and private plaintiffs against the trustees for the purposes of discovery.

On April 5, 1983, the district court denied the appellants' request for a jury trial in the actions against them. Judge Mishler held that with respect to the private plaintiffs' action the request was not timely and that with respect to the Secretary's action the appellants were not entitled to a jury trial because the action sought only equitable relief. The court also severed the appellants' third-party actions from the main claims against appellants and consolidated the latter for purposes of trial.

A bench trial was held before Judge Mishler on April 27-29, 1983. On plaintiffs' motion at the outset of the trial Judge Mishler limited the trial to the issue of the trustees' liability. During trial he excluded certain testimony during trial [sic] on the ground that it related to the question of damages rather than liability.

On July 21, 1983, Judge Mishler issued his decision and order finding that the trustees violated their fiduciary duty in making the Bancorporation loan and in failing to collect the unreimbursed expenses in connection with the Green loan. The court held the trustees jointly and severally liable for all losses incurred on account of those breaches of fiduciary duty. Three months later, on December 7,

1983, after a hearing on relief, Judge Mishler held the trustees liable for $2.5 million in damages on account of the Bancorporation loan and $30,599 on account of the Green loan.[5] He also removed the six trustees from their positions managing the Pension Fund.[6] The court noted that Cody was particularly unfit to serve as trustee because of his personal history of breaches of fiduciary duty[7] and that the other trustees were also unfit to serve because of their breaches of fiduciary duty in connection with the Bancorporation and Green loans.[8] The court appointed in their place an asset manager to oversee the Pension Fund's investments, and a fund manager to oversee the

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[5] The court below determined the loss as follows:

Unpaid balance	$1,625,000
Interest erroneously computed	32,500
Interest as provided in the loan agreement from 9/1/80 to 3/1/83	700,453
Interest from 3/1/83 to 12/15/83 at governing prime rate at 11%	141,512
SUB TOTAL	$2,499,465
Due Fund on failure to reimburse it for fees paid on the Green loan	23,473
Interest on the $23,473 at 9%	7,126
SUB TOTAL	$ 30,599
GRAND TOTAL	$2,530,064

[6] The trustees are composed of three appointed by the union and three appointed by the employers' association.

[7] Cody had been previously found guilty of violating the Racketeer Influenced and Corrupt Organizations Act, 18 U.S.C. §1961(5), in connection with his duties as a trustee and administrator of the Pension Fund. That conviction was affirmed by this court. *United States* v. *Cody*, 722 F.2d 1052 (2d Cir. 1983).

[8] Trustee Ralph Guercia was not serving at the time of the Hyman Green loan and hence he was removed as trustee solely on the basis of his participation in the Bancorporation loan.

Fund's day-to-day management. Both managers are to serve until March 31, 1985. On December 27, 1983, the court ordered that the trustees be removed from their positions with the Welfare, Annuity, and Legal Services Funds and that the asset and fund managers oversee those funds as well. Finally, on January 20, 1984, the court awarded $27,126 in attorneys' fees and $1,002 in costs to the private plaintiffs, and $9,416 in costs to the Secretary.

Discussion

The Severance of Appellants Third-Party Action, Denial of a Jury Trial of the Main Action, and Bifurcation of the Trial

Appellants argue that the district court erred in severing their third-party action, denying a jury trial of the consolidated actions against them, and bifurcating the trial into liability and damages phases. We disagree.

Fed. R. Civ. P. 42(b) vests the district court with broad discretion to sever a third-party claim for a separate trial. It provides that the district court *may* order a separate trial of a third party claim if such severance will be "in furtherance of convenience or to avoid prejudice, or when separate trials will be conducive to expedition and economy." In the present case the claims against the trustees were ready for trial whereas the third party claims were still early in discovery; indeed, not all of the third parties had been served, much less deposed or subjected to discovery requests. Thus, it was not an abuse of discretion for the court to sever those claims from the instant action. Moreover, there was no prejudice to the appellants on account of the severance. If they should prevail in their third-party claims, the amount of that recovery would be set off against any judgment entered against them by the district court.

The decision to bifurcate a trial into liability and damages phases likewise is "firmly within the discretion of the trial court under Fed. R. Civ. P. 42(b)." *In re Master Key Antitrust Litigation,* 528 F.2d 5, 14 (2d Cir. 1975). Bifurcation of the trial in the present case was reasonable because the two phases involved different types of evidence. The evidence in the liability phase was concerned with the prudence of the bank loan at the time when the loan was made whereas the damages phase involved evidence as to the amount of money eventually lost on account of the loan. Thus there was no abuse of discretion in bifurcating the trial.

Nor were appellants entitled to a jury trial of the claims against them since the plaintiffs seek equitable relief in the form of removal and restitution as distinguished from damages for wrongdoing or non-payment of benefits. There is no right to a jury trial of ERISA actions against pension fund trustees seeking the equitable remedy of restitution. *In re Vorpahl,* 695 F.2d 318, 320-22 (8th Cir. 1982); *Calamia* v. *Spivey,* 632 F.2d 1235, 1237 (5th Cir. 1980); *Wardle* v. *Central States, Southeast & Southeast Areas Pension Fund,* 627 F.2d 820, 829-30 (7th Cir. 1980), *cert. denied,* 449 U.S. 1112 (1981); *Rubin* v. *Decision Concepts, Inc.,* 566 F. Supp. 1057 (S.D.N.Y. 1983); Note, "The Right to Jury Trial in Enforcement Actions Under Section 502(a)(1)(B) of ERISA," 96 Harv. L. Rev. 737, 738 (1983).

Appellants rely on *Pollock* v. *Castrovinci,* 476 F. Supp. 606 (S.D.N.Y. 1979), *aff'd mem.,* 622 F.2d 575 (2d Cir. 1980), as authority for the proposition that they are entitled to a jury trial. In that case a plan beneficiary brought an action to obtain a share of the surplus of a terminated pension trust, and her recovery required a judicial reformation of the plan as amended. The district court held that once it decided the equitable question of whether a provision in the pension plan should be excised, the remaining question of whether the plaintiff was entitled to additional

monies was a legal question that should be decided by a jury. However, the legal or equitable nature of the latter question became moot, and there was no trial as to the amount plaintiff might recover, because the court determined that the plan should not be reformed. The order for a jury trial as to the amount of recovery could, of course, have been reconsidered by the district court at any time prior to the holding of such a trial; and, given what we view as the essentially equitable nature of Pollock's claim, we decline to follow the district court's mooted ruling that a jury trial was required. Accordingly, we hold that the district court correctly decided that appellants were not entitled to a jury trial.

The $2 Million Loan to Bancorporation

Appellants urge that the court below erred in finding that they breached their fiduciary duty under ERISA in connection with the Bancorporation loan. We disagree.

ERISA requires a pension fund fiduciary to act "solely in the interest" of a plan's participants and beneficiaries, and to discharge his duties "with the care, skill, prudence, and diligence . . . that a prudent man acting in a like capacity and familiar with such matters would use in the conduct of an enterprise of a like character. . . ." 29 U.S.C. §1104(a)(1)(B). If a trustee fails to adhere to these fiduciary standards, he may be held personally liable under ERISA for whatever losses result to a plan from his misconduct. 29 U.S.C. §1109(a).

Prudence is measured according to the objective "prudent person" standard developed in the common law of trusts. *Donovan* v. *Mazzola*, 716 F.2d 1226, 1231 (9th Cir. 1983), *cert. denied*, 104 S.Ct. 704 (1984); S. Rep. No. 127, 93d Cong., 2d Sess., *reprinted in* 1974 U.S. Code Cong. & Ad. News 4838, 4865 ("[t]he fiduciary responsibility section, in essence, codifies and makes applicable to these fi-

duciaries certain principles developed in the evolution of the law of trusts.") The court's task is to inquire "whether the individual trustees, at the time they engaged in the challenged transactions, employed the appropriate methods to investigate the merits of the investment and to structure the investment." *Donovan* v. *Mazzola,* 716 F.2d 1226, 1232 (9th Cir. 1983), *cert. denied,* 104 S.Ct. 704 (1984). *Donovan* v. *Cunningham,* 716 F.2d 1455, 1467 (5th Cir. 1983) ("courts have focused the inquiry under the 'prudent man' rule on a review of the fiduciary's independent investigation of the merits of a particular investment"). A trustee's lack of familiarity with investments is no excuse: under an objective standard trustees are to be judged "according to the standards of others 'acting in a like capacity and familiar with such matters.'" *Marshall* v. *Glass/Metal Association,* 507 F. Supp. 378, 384 (D. Hawaii 1980).

The court below found that the trustees acted in violation of the foregoing standard, and that they therefore are liable for the losses incurred by the Fund on the Bancorporation loan. That finding cannot be labelled clearly erroneous. On the contrary, evaluating the Bancorporation loan from the perspective of the "time of the investment decision" rather than from "the vantage point of hindsight," *American Communications Association* v. *Retirement Plan,* 488 F. Supp. 479, 483 (S.D.N.Y.), *aff'd,* 646 F.2d 559 (2d Cir. 1980), the finding was clearly correct. The trustees, being ill-equipped to evaluate the soundness of the proposed loan, failed to observe their duty to seek outside assistance. They relied exclusively on the representations of Bancorporation, the borrower, as to its financial strength and reached an investment decision after wholly inadequate inquiry and deliberation. A reasonable investigation would have revealed evidence that the loan was totally unsound. Although the expert called by the Secretary, John Duffy, had not, as appellants note, had experience in pension fund management, the issue here is

much more specialized, namely whether a loan to a bank or bank holding company was a prudent investment. Duffy was fully qualified by training and experience to testify on that basic issue and brought his expertise to bear through his analyses based on generally accepted ratios such as profitability, adequacy of capital, and liquidity, and through his evaluation of the asset quality of the borrower and its guarantor. These inquiries revealed that the loan was a loser from its inception. The district court properly relied on Duffy's testimony and its decision that the trustees acted imprudently in violation of ERISA must be affirmed.

The Unrecovered Expenses and Interest Incurred on Account of the Green Loan

Appellants argue that the district court erred in finding that they breached their fiduciary duty under ERISA in failing to recover over $23,000 plus interest in expenses incurred in connection with the Green loan. They challenge that finding on three grounds: (1) that the private plaintiffs, prior to the filing of this action, failed to make a demand on the trustees to seek recovery of the expenses; (2) that the private plaintiffs' claim is barred by the statute of limitations; and (3) that they have taken proper steps to recover the money from Green by counter-claiming against him for the expenses. We disagree.

With respect to the first claim, although common law may have required a prior demand before bringing an action, Congress did not incorporate that doctrine into the ERISA statute. The ERISA jurisdictional statute, 29 U.S.C. §1132(a)(3), contains no such condition precedent to filing suit. The claim must therefore be rejected.

Nor is the present action barred by the statute of limitations. The statute provides that a suit challenging a trustee's conduct must be filed within either six years of the date of the last action which constituted part of the breach of fiduciary duty *or* three years after the earliest

date on which the plaintiff had actual knowledge of the breach, whichever is earlier. 29 U.S.C. §1113.[9] Appellants argue that the private plaintiffs knew about the Green loan in February 1978, three and a half years before they filed this action in July 1981. However, the crucial commencement date for statute of limitations purposes is not the earliest date on which the plaintiffs could have learned that the trustees had approved the Green loan, but the earliest date on which they learned that the trustees would not recover all the costs incurred in negotiating the loan. Indeed, the parties stipulated that "the first time that Plaintiffs became aware that the Fund had expended money which was not repaid by Mr. Green was after the counterclaim was filed in the Green case." That counterclaim was filed in March 1981. The private plaintiffs' action, based on the trustees' failure to recover the costs incurred in connection with that loan, was filed a mere four months later. The district court therefore correctly ruled that the private plaintiffs' suit was timely filed.

Finally, appellants argue that because they have taken steps to recover the expenses incurred in making the Green

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[9] The statute provides in full:

"(a) No action may be commenced under this subchapter with respect to a fiduciary's breach of any responsibility, duty, or obligation under this part, or with respect to a violation of this part, after the earlier of—

(1) six years after (A) the date of the last action which constituted a part of the breach or violation, or (B) in the case of an omission, the latest date on which the fiduciary could have cured the breach or violation, or

(2) three years after the earliest date (A) on which the plaintiff had actual knowledge of the breach or violation, or (B) on which a report from which he could reasonably be expected to have obtained knowledge of such breach or violation was filed with the Secretary under this subchapter;

except that in the case of fraud or concealment, such action may be commenced not later than six years after the date of discovery of such breach or violation."

loan by filing a counterclaim against Green, which is presently pending before Judge Mishler, they should be excused from liability for those expenses. However, the possibility that they may recover from Green in the pending suit does not excuse them from liability as fiduciaries for losses incurred because of their own imprudent actions. If they should later recover the $30,474 in their action against Green, the district court will then credit them for that recovery in its order mandating that they compensate the Fund for losses caused by them.

The Relief Granted by the District Court

Appellants argue that the district court erred (1) in not reducing the $2.5 million judgment against them by the amount of monies received by the Fund from the sale of collateral and (2) in assessing prejudgment interest against them at the "prime-plus-one-percent" rate specified in the Bancorporation loan until March 1983, the loan's maturity date, and at the prime rate of 11% thereafter.

The first contention is answered by the district court's express provision that "[p]ayments received by the Fund on account of the loan will be credited against the judgment sum." As for the second, it is well-settled that ERISA grants the court wide discretion in fashioning equitable relief to protect the rights of pension fund beneficiaries including the award of prejudgment interest. *Donovan* v. *Bryans*, 566 F. Supp. 1258, 1264-65 (E.D. Pa. 1983); *Gilliam* v. *Eduardo*, 492 F. Supp. 1255, 1266-67 (E.D. Pa. 1980). This includes the power to award interest at a rate that will put the [Pension Fund] in the position that it would have occupied but for the [trustees'] breach." *Freund* v. *Marshall & Ilsley Bank*, 485 F. Supp. 629, 644 n.7 (W.D. Wis. 1979); *Gilliam* v. *Edwards*, 492 F. Supp. 1255, 1266-67 (E.D. Pa. 1980). Expert testimony revealed that at the time of the Bancorporation loan "several hun-

dred" other banking institutions were in the market to borrow at a rate of prime plus one percent. Awarding prejudgment interest in accord with prevailing interest rates is consistent with prior case law. *Donovan* v. *Mazzola*, 716 F.2d 1226, 1232-33 (9th Cir. 1983), *cert. denied*, 104 S.Ct. 704 (1984); *Freund* v. *Marshall & Ilsley Bank*, 485 F. Supp. 629 (W.D. Wis. 1979). Thus, the district court did not abuse its discretion.

Appellants, joined by the two intervenors, also challenge the district court's removal of the trustees in favor of a court-appointed asset manager and a fund manager as an abuse of the court's discretion to fashion equitable remedies. However, ERISA provides that:

> "Any person who is a fiduciary with respect to [a covered employee benefit] plan who breaches any of the responsibilities, obligations, or duties imposed upon fiduciaries by this subchapter . . . shall be subject to such other equitable or remedial relief as the court may deem appropriate." 29 U.S.C. §1109(a).

The accompanying legislative history expressly contemplated that such "other equitable or remedial relief" would include removal:

> "It is expected that a fiduciary . . . may be removed for repeated or substantial violations of his responsibilities and that upon removal the court may, in its discretion, appoint someone to serve until a fiduciary is properly chosen in accordance with the plan." S. Rep. No. 383, 93d Cong., 2d Sess., *reprinted in* 1974 U.S. Code Cong. & Ad. News 4890, 4989.

As we have held, removal of pension fund trustees and the appointment of a person to serve in their stead is appropriate under the statute when they have engaged in "repeated or substantial violation[s] of [their] responsibili-

ties." *Marshall* v. *Snyder*, 572 F.2d 894, 901 (2d Cir. 1978). Since the trustees here acted imprudently with respect to the Green loan and the Bancorporation loan, it was not an abuse of discretion for the court to remove the trustees pursuant to its equitable power.[10] The appointment of the asset and fund managers was therefore permissible and appropriate.

Judge Mishler's decision to appoint asset and fund managers also does not in our view violate the Labor Management Relations Act ("LMRA"). It is true that under §302(c)(5) of the LMRA, 29 U.S.C. §186(c), employees and employers of a pension fund must be represented in the administration of the fund and this provision has been interpreted by the Supreme Court to require an equal balance in the representation. *NLRB* v. *Amax Coal Company*, 453 U.S. 322, 330 (1981). However, although the union has appointed its successor trustees and the employer association is prepared to do likewise, we are satisfied that these provisions of the LMRA are subject to the broad equitable powers granted by ERISA to remedy breaches of trust on the part of the representatives by appointment of managers for a reasonable length of time. Otherwise the union and employers could thwart the objectives of ERISA by reappointing the same derelict representatives to continue the violations of their fiduciary duties.

A more difficult question is whether the 15-month term during which the asset manager and fund manager were appointed to serve exceeds the authority of the district court under ERISA. The statute does not expressly deal with the matter. However, the legislative history of

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[10] Although trustee Guercia acted imprudently only with respect to the Bancorporation loan, his removal as trustee is justified on the basis that it would be infeasible to allow him to maintain his position while removing the other trustees in favor of a court-appointed asset manager and fund manager.

ERISA states that upon removal of fiduciaries "the court may, in its discretion, appoint someone to serve until a new fiduciary is properly chosen in accord with the plan." S. Rep. No. 383, 93d Cong., 2d Sess., *reprinted in* 1974 U.S. Code Cong. & Ad. News 4890, 4989. Congress' intent thus appears to have been that the court should not unduly prolong the duration in office of a receiver or other officer appointed by it but make an effort to turn over control to trustees elected as permitted under ERISA provided they appear to the court to meet appropriate standards of integrity and competence. Although in *Marshall* v. *Snyder*, 572 F.2d 894, 896 (2d Cir. 1978), we approved the appointment of a receiver by the district court until new trustees could be installed, we have not ruled on the issue of whether a receiver or other officer may be appointed to serve beyond the date when newly elected trustees are installed. In the present case the risk of further harm to the beneficiaries, in light of the past trustees' derelictions, lies in the area of investment management, presently conducted by the court-appointed asset manager rather than in the day-to-day operation of the fund including supervision of disbursements and receipts, which is presently carried out by the fund manager. The latter operation involves little discretion and there is no claim that the trustees, once the imprudent investment decisions were made, improperly accounted for pension fund, including supervision of disbursements and receipts, the district court's appointment of the asset or investment manager until March 31, 1985, as a legitimate and appropriate exercise of its equitable power. With respect to the appointment of the fund manager, however, we remand to the district court for further consideration in light of the foregoing, with instructions to terminate the appointment of the fund manager as soon as successor trustees are appointed by the union and employer association who meet with the court's approval, even if that occurs prior

to March 31, 1985. See *Donovan* v. *Mazzola*, 716 F.2d 1226, 1237 (9th Cir. 1983), *cert. denied*, 104 S.Ct. 722 (1984) (appointment of investment manager to oversee pension fund for 10 years approved on condition that non-investment functions would be performed by trustees).

The intervenor Local 282 argues that the asset manager chosen by the district court, Albert Lewis, is not a registered investment adviser under the Investment Advisers Act of 1940 as required by the ERISA statute[11] and that therefore he is not qualified to serve as an asset manager. The intervenor, however, has misconstrued the statute, which provides that an employee benefit plan *may* provide for the appointment of an "investment manager" to manage the assets of the plan, 29 U.S.C. §1102(c)(3), in which event the trustees will not be liable for the acts or omissions of such investment manager. 29 U.S.C. §1105(d). In order to shield the trustees from liability in this fashion, the investment manager must meet the requirement set forth in 29 U.S.C. §1002(38), including the requirement that the investment manager be a registered investment manager under the Investment Advisers Act of 1940. However, the statute does not require that asset managers appointed by the district court satisfy these

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[11] Title 29 U.S.C. §1002(38). This definitional section provides in full:

> "(38) The term 'investment manager' means any fiduciary (other than a trustee or named fiduciary, as defined in section 1102(a)(2) of this title)—
>
> (A) who has the power to manage, acquire, or dispose of any asset of a plan;
>
> (B) who is (i) registered as an investment adviser under the Investment Advisers Act of 1940; (ii) is a bank, as defined in that Act; or (iii) is an insurance company qualified to perform services described in subparagraph (A) under the laws of more than one State; and
>
> (C) has acknowledged in writing that he is a fiduciary with respect to the plan."

criteria. On the contrary, the district court possesses greater latitude in appointing asset managers. The intervenor has not alleged that the chosen asset manager is any way ill-equipped to serve in that capacity. We defer to the discretion of the court below in making that appointment.

We have considered the other grounds for reversal urged by appellants and find them to be without merit. Judge Mishler was not obligated to recuse himself simply because he presided at the criminal trial of Cody arising out of Cody's activities as a trustee of the Pension Fund. Recusal under 28 U.S.C. §455(b) for bias or prejudice based on personal knowledge of disputed evidentiary facts is required if that "[i]nformation or knowledge possessed by a judge . . . stem[s] from an extrajudicial source." *United States* v. *Coven*, 662 F.2d 162, 168 (2d Cir. 1981), *cert. denied*, 456 U.S. 916 (1982). "Knowledge acquired by a judge while he performs judicial duties does not constitute grounds for disqualification." *Id.* Here the information forming the basis of the bias claim came to Judge Mishler's attention in his performance of his duties in the prior judicial proceeding.

Accordingly, we affirm the judgment of the district court in all respects with the exception of the appointment of the fund manager and remand with directions to terminate that appointment upon the parties' designation of trustees in accordance with the plan who are found by the district court to meet the foregoing requirements.

Order of United States District Court

UNITED STATES DISTRICT COURT

EASTERN DISTRICT OF NEW YORK

81 CV 2277

December 28, 1982

TED KATSAROS, JOHN KUEBLER, ROBERT TROTT, LAWRENCE KUDLA, and CHARLES CURD, as participants in the Teamsters Local 282 Pension Trust Fund,

Plaintiffs,

—against—

JOHN CODY, ROBERT SASSO, JOHN DEE, WILLIAM ARGENTO, RALPH GUERCIA, HERBERT SCHNEIDER and LOUIS NAPPI, as Trustees of Teamsters Local 282 Pension Trust Fund,

Defendants.

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82 CV 1920

RAYMOND J. DONOVAN, Secretary of the United States Department of Labor,

Plaintiff,

—against—

JOHN CODY, WILLIAM ARGENTO, JOHN DEE, RALPH GUERCIA, LOUIS G. NAPPI, ROBERT SASSO, HERBERT SCHNEIDER and the Teamsters Local 282 Pension Trust Fund,

Defendants.

MISHLER, *District Judge:*

Plaintiffs Katsaros, Kuebler, Trott, Kudla and Curd, participants in the Teamsters Local 282 Pension Trust

Fund (the "Trust Fund"), brought suit against certain named Trustees of the Trust Fund. (81 CV 2277). Such plaintiffs now move, pursuant to Rule 42, Fed. R. Civ. P., to consolidate the above referenced actions for all purposes, including trial. The second action (82 CV 1920) is brought by the Secretary of the United States Department of Labor against the same named defendant Trustees of the Trust Fund. The two actions involve common questions of law and fact.

The motion is granted to the extent that these actions shall be consolidated for all pre-trial discovery matters. We reserve decision on the issue of consolidation for the purpose of trial. The parties are invited to advise the court as to the results of pre-trial discovery proceedings that bear on the question of consolidation for trial, and it is

So Ordered.

Dated: Uniondale, New York
December 28, 1982

Jacob Mishler
U. S. District Judge

The clerk of the court is directed to consolidate case 82 CV 1920 with case 81 CV 2277 in accordance with this decision.

Memorandum of Decision and Order dated April 5, 1983

UNITED STATES DISTRICT COURT

EASTERN DISTRICT OF NEW YORK

CV 81-2277

TED KATSAROS, et al.,

Plaintiffs,

—against—

JOHN CODY, et al.,

Defendants.

JOHN CODY, et al.,

Third-Party Plaintiffs,

—against—

ANTHONY G. ANGELOS, et al.,

Third-Party Defendants.

TEAMSTERS LOCAL 282 PENSION TRUST FUND,

Second Third-Party Plaintiff,

—against—

ANTHONY G. ANGELOS, et al.,

Second Third-Party Defendants.

Memorandum of Decision and Order
dated April 5, 1983

CV 82-1920

RAYMOND J. DONOVAN, Secretary of the United States Department of Labor,

Plaintiff,

—against—

JOHN CODY, et al.,

Defendants.

JOHN CODY, et al.,

Third-Party Plaintiffs,

—against—

ANTHONY G. ANGELOS, et al.,

Third-Party Defendants.

TEAMSTERS LOCAL 282 PENSION TRUST FUND,

Second Third-Party Plaintiff,

—against—

ANTHONY G. ANGELOS, et al.,

Second Third-Party Defendants.

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Memorandum of Decision and Order
dated April 5, 1983

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MISHLER, *District Judge*

In February and March of 1979 the trustees of the Teamsters Local 282 Pension Trust Fund ("Trustees"), approved and disbursed a loan of 2 million dollars to the

Memorandum of Decision and Order dated April 5, 1983

Des Plains Bancorporation, Inc. ("Bankcorporation"), a bank holding company. The loan was secured by all the stock in the Des Plains Bank ("Bank"), a wholly-owned subsidiary of Bankcorporation. Following the closing of the Bank by federal and state regulatory officials on March 14, 1981, two separate actions were brought against the Trustees alleging violation of fiduciary duties under the Employee Retirement Income Security Act of 1974 ("ERISA"), 29 U.S.C. § 1101, et seq. The Teamsters Local 282 Pension Trust Fund ("Fund") has been joined as a defendant. These actions, which have been consolidated for pre-trial matters, are referred to here as the Katsaros action and the Donovan action. The Trustees and the Fund have brought separate third-party actions against the named directors of Bankcorporation ("Directors"). Several pre-trial motions are now before the court.

I. Plaintiffs in Each Case Move to Strike the Jury Demand

Katsaros, et al. v. Cody, et al.

Participants in the Teamsters Local 282 Pension Plan under the Fund instituted an action by filing a complaint in the Office of the Clerk of the Court against the Trustees on July 14, 1981. The complaint alleged that the Trustees breached their fiduciary duties in violation of Sections 404(a)(1)(B) and (C) of ERISA, 29 U.S.C. § 1104(a)(1) B and C.[1] The claim is based on an agreement made by

[1] Section 1104(a)(1) provides in pertinent part:

(a) *Prudent man standard of care.*

[A] fiduciary shall discharge his duties with respect to a plan solely in the interest of the participants and beneficiaries and—

(A) for the exclusive purpose of:

(footnote continued on following page)

the Trustees on June 7, 1981 to loan one Hyman Green 20 million dollars for the construction of a hotel and gambling casino in Las Vegas, Nevada[2] and the loan made by the Trustees to Bankcorporation in the amount of 2 million dollars. The complaint seeks removal of the Trustees from their position of trust, restitution,[3] and punitive damages. All Trustees answered by O'Connor & Mangan, P.C. by service of the answer on plaintiffs' attorney on October 27, 1981. Neither party demanded a jury trial.

On August 17, 1982, the firm of Hall, McNicol, Hamilton, Clark & Murray was substituted as counsel for the Trustees. On December 20, 1982 the parties entered into a stipulation authorizing the amendment to the complaint by adding "Local 282 Pension and Welfare Fund as a defendant." On January 6, 1983, the firm of Wilson, Elser, Edelman & Dicker was substituted as counsel for the

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(footnote continued from previous page)

> (i) providing benefits to participants and their beneficiaries; and
>
> (ii) defraying reasonable expenses of administering the plan;
>
> (B) with the care, skill, prudence and diligence . . . that a prudent man acting in a like capacity and familiar with such matters would use in the conduct of an enterprise of a like character and with like aims;
>
> (C) by diversifying the investments of the plan so as to minimize the risk of large losses, unless under the circumstances it is clearly prudent not to do so.

[2] The loan was enjoined on complaint of the Secretary of Labor, *Marshall* v. *Teamsters Local 282 Pension Trust Fund,* 458 F. Supp. 986 (E.D.N.Y. 1978).

[3] Plaintiffs seek restitution on behalf of the Fund of certain unrecovered expenses respecting the Las Vegas transaction and the outstanding amount due the Fund under the Des Plains loan agreement.

Trustees. An amended complaint was filed in the Office of the Clerk of the Court on January 13, 1983. The only change involved (1) the caption and (2) the addition of paragraph 5 describing the Fund as an employee benefit plan under Section 3(2) of ERISA, 29 U.S.C. § 1002(2). On January 24, 1983, counsel for the Trustees served an answer to the amended complaint, together with a jury demand by mail. On February 2, 1983, the Fund answered by O'Connor & Mangan, P.C. The Fund did not demand a trial by jury.

Donovan v. *Cody, et al.*

The Secretary of Labor filed a complaint on July 1, 1982 in the Office of the Clerk of the Court against the Trustees alleging that the loan to Bankcorporation violated 29 U.S.C. § 1104(a)(1) A and B.[4] The Secretary seeks equitable relief including restitution of the amount outstanding under the Des Plains loan agreement, removal of the Trustees as fiduciaries of the Fund and the appointment of a manager for the purpose of administering the Fund. The complaint was amended by stipulation on September 28, 1982 by adding the Fund as a party defendant. Trustees answered on November 4, 1982 and served a jury demand requesting "a trial by jury on all issues raised herein" on November 12, 1982. The Fund answered by O'Connor and Mangan, P.C. on November 19, 1982. The Fund made no demand for a trial by jury.

Rule 38(b), Fed.R.Civ.P., requires that a party seeking "a trial by jury of any issue triable of right by a jury" serve a demand "not later than 10 days after service of the last pleading directed to such issue." A failure to make such demand constitutes a waiver. Rule 38(d), Fed.R.

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[4] See Note 1, supra.

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Civ.P. Once the right is lost as to the issues framed by the pleadings, it is not revived as to those issues through amendment of the pleadings. *Lanza* v. *Drexel & Co.*, 479 F.2d 1277 (2d Cir. 1973). In *Lanza, supra,* the claim alleged a violation of Section 10(b) of the Securities Exchange Act of 1934, 15 U.S.C. § 78j(b), and S.E.C. Rule 10(b)-5. After having effectively waived the right to a jury trial by failing to timely make such demand, plaintiffs amended the original complaint by adding an allegation that the prospectus, which constituted one of the instruments of the alleged fraud, was false on the date of issue. The court held:

> Under Rule 38(d) the failure to demand a jury trial within the period designated by Rule 38(b) constitutes a waiver of that right as to all issues raised by the complaint. If the original complaint is subsequently amended, the right to demand a jury trial is revived in an action such as this only if the amendment changes the issues. *Western Geophysical Co. of America, Inc.* v. *Bolt Associates, Inc.*, 440 F.2d 765, 769 (2d Cir. 1971).
>
> The amendments did not raise new issues within the meaning of Rule 38 such as would entitle Kircher to demand a jury trial as of right. The case involved, and the original complaint raised, one basic issue: Whether plaintiffs were fraudulently induced to exchange their Victor stock. Kircher's failure to demand a jury trial waived his right as to all issues relating to this general area of dispute.

Id. at p.1310. *See also Bell* v. *Cameron Meadows Land Co.*, 669 F.2d 1278, 1285 (9th Cir. 1982), *Walton* v. *Eaton Corp.*, 563 F.2d 66, 71-72 (3rd Cir. 1977), 9 Wright & Miller, Federal Practice and Procedure § 2321, (1971).

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The issues after amendment of the Katsaros complaint were the same as before amendment. The amendment did not restore the right to trial by jury. We find that such right was waived.

Turning to the Donovan complaint, it is clear that the Secretary seeks only equitable relief.[5] "[T]he right of trial by jury . . . does not extend to cases of equity jurisdiction. If it be conceded or clearly shown that a case belongs to this class, the trial of questions involved in it belongs to the court itself, no matter what may be its importance or complexity." *Katchen* v. *Landy,* 382 U.S. 323, 337, 86 S. Ct. 467, 477 (1966) quoting *Barton* v. *Barbour,* 104 U.S. 126, 133-34, 26 Law Ed. 672, 676 (1881). In classifying issues or claims as either legal or equitable we look to the traditional or historical manner of viewing them and the remedy sought. *See e.g., Dimick* v. *Schiedt,* 293 U.S. 474, 476, 55 S. Ct. 296, 297 (1935); *Baltimore & Carolina Line, Inc.* v. *Redman,* 295 U.S. 654, 55 S. Ct. 890 (1935). *See also Swofford* v. *B & W, Inc.,* 336 F.2d 406, 409 (5th Cir. 1964). The usual proceedings

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[5] The government's brief reports from the legislative history of ERISA, the Congressional intent to retain the traditional form of equitable relief in the enforcement of fiduciary obligations under ERISA as follows:

> Appropriate equitable relief may be granted in a civil action. For example injunctions may be granted to prevent a violation of fiduciary duty, and a constructive trust may be imposed on the plan assets, if needed to protect the participants and beneficiaries. Also the bill provides that a fiduciary may be removed through a civil action brought by the Secretary or participants or beneficiaries if he has violated any of the specified fiduciary obligations, or is serving in violation of the criminal conviction provisions.

S. Rep. No. 303, 93rd Cong., 1st Sess. 105-06 (1973), reprinted in I. Legislative History of the Employees Retirement Income Security Act of 1974, 94th Congr., 2d Sess. 1173-74 (Comm. Print 1976).

for the removal of the trustee is by a bill in equity. Bogert, Trusts & Trustees (2d ed. 1978) § 524.

The Secretary of Labor seeks judgment directing the Trustees to reimburse the Fund for any losses which the Fund incurred by reason of their breaches of fiduciary duty. Such money request does not necessarily convert a non-jury claim into a jury claim. *Swofford* v. *B & W., supra,* 336 F.2d at 414. The nature of the Donovan action is the same as the Katsaros claim, i.e., beneficiaries of a trust seeking equitable relief. Such claims are traditionally within the exclusive jurisdiction of equity. *Nedd* v. *United Mine Workers,* 556 F.2d 190, 207 (3rd Cir. 1977), *cert. denied,* 434 U.S. 1013, 98 S. Ct. 727 (1978); *Local No. 92, International Association of Bridge, Structural and Ornamental Iron Workers* v. *Norris,* 383 F.2d 735, 740-41 (5th Cir. 1967); *Dixon* v. *Northwestern National Bank,* 297 F. Supp. 485, 488 (D. Minn. 1969). *See* 1 Restatement of Trusts (2d ed. 1959) § 199. We conclude that the right to trial by jury does not apply to the Donovan action.

The Third-Party Complaints

The Trustees and the Fund served third-party complaints against the Directors alleging fraud and misrepresentation in both the Katsaros action and the Donovan action. The complaints allege, *inter alia,* claims based on Section 17(a) of the Securities Act of 1933, 15 U.S.C. § 77q(a); Section 10(b) of the Securities Act of 1934, 15 U.S.C. § 78j(b) and Securities Exchange Rule 10(b)-5, fraud and negligence.[6] Defendants argue that the fact

[6] In an attempt to show common issues of fact with those raised in the underlying complaints, the third-party complaints also allege a violation of Section 404(a)(1) A and B of ERISA; 29 U.S.C. § 1104(a)(1) (A) and (B) in that: "The Directors knowingly participated in the alleged breach of the Trustees fiduciary obligations described in the . . . amended complaint[s]."

issues in the third-party complaints, which are triable before a jury, are the same issues raised in the Katsaros and Donovan complaints. Defendants insist that the issues raised in the Katsaros and Donovan ERISA claims must therefore be tried before a jury, citing *Beacon Theatres, Inc.* v. *Westover,* 359 U.S. 500, 79 S. Ct. 948 (1959).

Plaintiffs move for severance of the third-party claims. Defendants oppose the motions; but argue that if granted, the basic claims must be tried to a jury. We grant the motion for severance, as discussed separately below. Accordingly, we examine the relationship between the equitable claims in the ERISA actions and the legal claim in the third-party actions.

The principle is well established that issues common to both legal and equitable claims must be tried to a jury and the court must defer to the prior determination of the legal claim before deciding the equitable claims. *Ross* v. *Bernard,* 396 U.S. 531, 537-38, 90 S. Ct. 733, 738 (1970); *Dairy Queen, Inc.* v. *Wood,* 369 U.S. 469, 472-73, 82 S. Ct. 894, 896-97, (1962); *Beacon Theatres, Inc.* v. *Westover, supra,* 359 U.S. at 511, 79 S. Ct. at 957.

The issues in the actions against the Trustees are not the same as the issues in the third-party actions. The Secretary's complaint clearly sets forth his theory of liability under § 1104(a); i.e., the trustees failed to (a) analyze the financial condition of the borrower, (b) determine the adequacy of the collateral, (c) inquire as to the application of the proceeds of the loan, and (d) require terms and conditions that would protect the Fund. The Trustees argue that evidence of fraudulent and negligent conduct on the part of the Directors will be offered to show that the Trustees acted "with the care, skill, prudence and diligence under the circumstances then prevail-

ing, that a man acting in a like capacity . . . would use," as required by 29 U.S.C. § 1104(a)(1)(B).

In *Tucker* v. *Arthur Andersen & Co.*, 646 F.2d 721 (2d Cir. 1981) a purchaser of securities stated a claim of securities fraud against the accountant for the corporation. The accountant filed a third-party complaint for indemnification or contribution alleging that one Meckler and others concealed information of embezziement (the basis of the fraud claim against the accountant) from the accountant. In a prior action, lending institutions sued Meckler and others alleging that Meckler knew of the embezzlement and owed a special duty to the lending institutions to disclose the information. The court in *Tucker* reversed the lower court's granting of summary judgment, basing its decision on collateral estoppel and issue preclusion. The court stated:

> The fact that several operative facts may be common to successive actions between the same parties does not mean that a judgment in the first will always preclude litigation of the second. Whether or not the first judgment will have preclusive effect depends on whether a different judgment in the second action would impair rights or interests created by the first judgment, whether the same evidence is necessary to support both claims, and whether the essential facts in the second were present in the first (citations omitted).
>
> On the surface, Andersen's claims against Meckler in the *State Mutual* action and the present action appear to be the same. The language of the claims in both actions asserts that Meckler is liable to Andersen by reason of his "fraud and deceit upon Andersen". . . . Although much of the evidence on the

two sets of claims would overlap, the factual matrices to be proven by the two groups are not identical.

646 F.2d at 727-28.

We find that the issues to be tried to a jury in the third-party actions do not require that the non-jury issues of the ERISA actions be tried to a jury as well. The principle enunciated in *Beacon Theatres* and *Ross* is inapplicable here. Plaintiffs' motions to strike the jury demands are granted.

II. Summary Judgment

Motions for summary judgment are made by plaintiffs, Trustees and third-party defendants.[7] Before discussing each motion we note the oft-repeated recognized principles governing summary judgment motions.

The moving party has the burden of showing that there is no genuine issue of material fact. Rule 56(c) Fed.R. Civ.P., *Adickes* v. *S. H. Kress & Co.*, 398 U.S. 144, 157, 90 S. Ct. 1598, 1608 (1970); *United States* v. *One Tintoretto Painting, etc.*, 691 F.2d 603, 606 (2d Cir. 1982). The moving party has the initial burden of presenting "evidence on which, taken by itself, it would be entitled to a directed verdict." *Donnelly* v. *Guion*, 467 F.2d 290, 293 (2d Cir. 1972). The party opposing summary judgment must then "set forth specific facts showing that there is a genuine issue for trial." Rule 56(e) Fed.R.Civ.P. All ambiguities must be resolved and all inferences drawn from the underlying facts must be "in the light most favorable to the party opposing the motion. . . . Uncertainty as to the true state of any material fact de-

[7] The motions by third-party defendants directed to the complaint will be decided in a separate opinion.

feats the motion." *United States* v. *One Tintoretto Painting, etc., supra* at 606.

A. *Plaintiffs' Motions for Summary Judgment*

The critical issue in the Katsaros and Donovan complaints is whether the Trustees violated their statutory duty under 29 U.S.C. § 1104(a) in failing to discharge their duties "solely in the interest of the participants and beneficiaries" of the Fund, and "with the care, skill, prudence and diligence under the circumstances then prevailing that a prudent man acting in a like capacity and familiar with such matters would use in the conduct of an enterprise of a like character and with like aims."

The Trustees do not challenge the statement of facts as set forth by the government.[8] The Trustees claim that Angelos and Howe, third-party defendants, convinced the Trustees that the Bank was financially sound, that it was suffering from a short-term cash flow problem, but was operating at a profit. The Trustees set forth other facts in support of their allegedly prudent decision, *e.g.*, Herb

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[8] The government shows that defendant Cody placed the matter of the Bankcorporation loan on the agenda of the Trustees meeting for February 27, 1979 without prior notice. None of the other Trustees were aware of the proposal prior to the meeting or knew of the existence of the borrower. Angelos (president and chairman of the board of Bankcorporation and the Bank), and Howe (director of Bankcorporation and the Bank and also a partner in the law firm of Jenner & Block, counsel to the bank) attended the meeting. The loan was approved after discussion of an hour or two. The Trustees were unfamiliar with the financial statements of banks and lacked the skill to analyze them. They did not seek expert financial advice. Angelos and Howe advised the Trustees of the bank's cash-flow problems. Cody and another trustee, Guercia, went to Chicago on February 28, 1979 to examine the real estate offered as collateral. On March 1, 1979, Cody and Guercia executed the loan agreements.

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Bolin, Esq., attorney for the Fund, retained Chicago counsel to represent the Fund; Cody and Guercia viewed the real estate offered as collateral to Angelos' personal guarantee; the Trustees received all the issued stock of the Bank as collateral.

The statutory standard presents a question of fact that does not readily lend itself to summary judgment. The care, skill and prudence of "a prudent man acting in a like capacity" in granting a loan might very well depend on the amount of the loan, the class of borrower, custom and usage in making such loans, etc. What the Trustees knew, should have known and the effort or lack of effort to acquire the necessary information would be relevant to the issue presented. *Home Insurance Co.* v. *Aetna Casualty & Surety Co.*, 528 F.2d 1388 (2d Cir. 1976) (Question as to the custom of insurance industry in interpreting the "batch clause" in an insurance policy precluded the grant of summary judgment.) *Sherman* v. *British Leyland Motors, Ltd.*, 601 F.2d 429 (9th Cir. 1979) (Though the claim and defense were clearly defined by documents, questions of motive, purpose and economic effect precluded summary judgment in antitrust action).

Plaintiffs' motions for summary judgment are denied.

B. *Trustees' Motions for Summary Judgment*

Trustees' motion for summary judgment is directed to (1) the "First Cause of Action" alleged in the Katsaros complaint and (2) the demand for punitive damages. Defendant trustee Guercia moves to dismiss the first claim as to him on the ground that he did not become a trustee until October 24, 1978 and indeed after the events alleged in the First Cause of Action had transpired. Guercia's motion is granted.

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1. Statute of Limitations

The complaint in the Katsaros action was filed on July 14, 1981. The First Cause of Action alleged that on or about November 15, 1977, the Trustees agreed to loan one Hyman Green 20 million dollars for the construction of a hotel and gambling casino in Las Vegas, Nevada. The loan was enjoined on motion of the Secretary of Labor on August 11, 1978. *Marshall* v. *Teamsters Local 282 Pension Trust Fund,* 458 F. Supp. 986 (E.D.N.Y. 1978). The loan agreement provided that Green would pay the expenses of the loan, including attorney fees. The complaint states that the Fund expended sums in excess of 100 thousand dollars in connection with the prohibited loan and seeks reimbursement. The answer to the complaint failed to allege the statute of limitations as an affirmative defense. The Trustees stated, in the answer to the "First Amended Complaint," that Green was obligated to pay all costs; that the "reimbursement expenses came to $73,473.77; that Green reimbursed the Fund in the sum of $50,000 and that the Fund is currently suing Green for the balance of $23,473.57." (Answer par. 8).

Katsaros argues (1) that the defense was waived by failure to assert it in the original answer, Fed.R.Civ.P. 8(c) and (2) that pursuant to Section 413 of ERISA, 19 U.S.C. § 1113, the claim carries a six year limitation and not a three year limitation.

Rule 8(c) must be read together with Rule 15(a) which provides in pertinent part: "a party may amend his pleading . . . by leave of the court . . . and leave shall be freely given when justice so requires." *Henry* v. *First National Bank of Clarksdale,* 595 F.2d 291, 298 (5th Cir. 1979), *cert. denied,* 444 U.S. 1074, 100 S. Ct. 1020 (1980) (Assertion of res judicata and collateral estoppel defenses raised for the first time *on appeal* were considered "waived if not pleaded in the trial court") cited by Katsaros does not

support waiver of the affirmative defense. *Zenith Radio Corp.* v. *Hazeltine,* 401 U.S. 321, 91 S. Ct. 795 (1971). We do not find that the defense was waived.

Section 1113 provides, in relevant part, as follows:

> (a) No action may be commenced . . . with respect to a fiduciary's breach of any responsibility, duty, or obligation under this part, or with respect to a violation of this part, after the earlier of—
>
> (1) six years after (A) the date of the last action which constituted a part of the breach or violation, or (B) in the case of an omission, the latest date on which the fiduciary could have cured the breach or violation, or
>
> (2) three years after the earliest date (A) on which the plaintiff had actual knowledge of the breach or violation, or (B) on which a report from which he could reasonably be expected to have obtained knowledge of such breach or violation was filed with the Secretary under this subchapter;
>
> except that in the case of a fraud or concealment, such action may be commenced not later than six years after the date of discovery of such breach or violation.

The complaint alleged a breach of the Trustees' fiduciary duty in the expenditure of the Fund's money "in the arrangement and defense of a transaction" and the failure to reimburse the Fund. Katsaros claims that plaintiffs could not have known of the expenditures until the entry of judgment on August 11, 1978 or of the Trustees violation in failing to obtain reimbursement at a time subsequent thereto. The Katsaros plaintiffs argue that the three year limitation set forth at 29 U.S.C. § 1113(a)(2) is measured with respect to August 11, 1978 or a date thereafter.

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The issue of knowledge in order to determine the limitation period is not usually capable of resolution on affidavits. *Schmidt* v. *McKay,* 555 F.2d 30 (2d Cir. 1977); *Schoenbaum* v. *Firstbrook,* 405 F.2d 215 (2d Cir. 1968), *cert. denied, sub nom, Manley* v. *Schoenbaum,* 395 U.S. 906, 89 S.Ct. 1747 (1969). The Trustees' motion to dismiss the First Cause of Action is denied.

2. Punitive Damage Claim

The only reference to punitive damages in the Katsaros complaint is found in the prayer for relief (Par. 4). No basis for the claim is stated. Punitive damages are not recoverable under ERISA for a violation of a fiduciary duty imposed on a trustee. *Dependahl* v. *Falstaff Brewing Corp.,* 653 F.2d 1208, 1216 (8th Cir.), *cert. denied, sub nom, Dependahl* v. *Kalmanovitz,* —— U.S. ——, 102 S. Ct. 641 (1981). The Trustee's motion to dismiss the claim for punitive damages is granted.

III. Trustees' Motion and the Fund's Motion to Dismiss Under Rule 12(b)(7)

At a time before the Fund was joined as a party, the Trustees moved to dismiss for "failure to join a party under Rule 19" (Rule 12(b) (7)). Subsequently, the Fund appeared and answered alleging, *inter alia,* failure to join indispensable parties as an affirmative defense. The Fund then moved to dismiss the complaint under Rule 12(b)(7) for failure to join the directors of the Des Plaines Bank-corporation.

Complete relief can be granted plaintiffs in both actions without the presence of the Directors. They are neither indispensable nor necessary parties. *See Herpich* v. *Wallace,* 430 F.2d 792, 817 (5th Cir. 1970). But even if full relief could not be granted because of the absence of the

Directors as contended by the Fund, the answer is not dismissal. "Rule 19 calls for a pragmatic approach; simply because some forms of relief might not be available due to the absence of certain parties, the entire suit should not be dismissed if meaningful relief can still be accorded." *Smith* v. *United Brotherhood of Carpenters and Joiners,* 685 F.2d 164, 166 (6th Cir. 1982).[9]

IV. Plaintiffs' Motion to Sever the Third-Party Claims

Plaintiffs move pursuant to Rule 14(a) to sever the third-party claims.

Both sides in the Katsaros and Donovan actions advised the court that all pretrial discovery has been completed and they are ready for trial. The third-party actions are still in a preliminary stage. Not all third-party defendants have been served with process. The third-party defendants who were served (Howe, Jensen, Karkazis and Kirie) have not answered. By motions these third-party defendants challenge the in personam jurisdiction of the court. The third-party complaints charge, *inter alia,* violations of Section 22(a) of the Securities Act, 15 U.S.C. § 77v(a), Section 27 of the Exchange Act, 15 U.S.C. § 78aa and common law fraud[10]—issues unrelated or of doubtful relevancy to the issues in the basic actions. The delay occasioned by the trials on the third-party complaints will substantially prejudice the rights of the plaintiffs. Additionally, a decision dismissing the Katsaros and Donovan complaints would end the third-party claims. *See Garber* v. *Randell,* 477 F.2d 711, 714 (2d Cir. 1973). The motions for separate trials are granted.

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[9] We note that the question of the in personam jurisdiction of this court over the non resident directors has not been resolved. We assume for these purposes that jurisdiction cannot be acquired over all the directors.

[10] See Note 6, *supra.*

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V. The Trustee's Motion for a Stay

The Trustees seek a stay of the Katsaros and Donovan trials to afford them the opportunity to pursue recovery of the alleged losses. For the reasons stated above respecting plaintiffs' motions to sever the third-party claims, the motion for a stay is denied.

VI. Joint Trial

The court finds that *Katsaros, et al.* v. *Cody, et al.* (CV 81-2277) and *Donovan* v. *Cody, et al.* (CV 82-1920) present common questions of law and fact. The actions are consolidated for trial. Rule 42(a). Trial shall commence on Monday, April 25, 1983 at 10:00 a.m.

The decisions herein made are,

So Ordered.

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U.S.D.J.

Memorandum of Decision and Order dated April 15, 1983

UNITED STATES DISTRICT COURT

EASTERN DISTRICT OF NEW YORK

CV 81-2277

TED KATSAROS, et al.,

Plaintiffs,

—against—

JOHN CODY, et al.,

Defendants.

JOHN CODY, et al.,

Third-Party Plaintiffs,

—against—

ANTHONY G. ANGELOS, et al.,

Third-Party Defendants.

TEAMSTERS LOCAL 282 PENSION TRUST FUND,

Second Third-Party Plaintiff,

—against—

ANTHONY G. ANGELOS, et al.,

Second Third-Party Defendants.

Memorandum of Decision and Order
dated April 15, 1983

CV 82-1920

RAYMOND J. DONOVAN, Secretary of the United States Department of Labor,

Plaintiff,

—against—

JOHN CODY, et al.,

Defendants.

JOHN CODY, et al.,

Third-Party Plaintiffs,

—against—

ANTHONY G. ANGELOS, et al.,

Third-Party Defendants.

TEAMSTERS LOCAL 282 PENSION TRUST FUND,

Second Third-Party Plaintiff,

—against—

ANTHONY G. ANGELOS, et al.,

Second Third-Party Defendants.

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Memorandum of Decision and Order
dated April 15, 1983

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Memorandum of Decision and Order
dated April 15, 1983

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MISHLER, *District Judge*

Defendants move to reargue the court's memorandum of decision and order dated April 5, 1983 and for recusal under 28 U.S.C. § 455, and in the event they are unsuccessful in their application, to certify the question to the Second Circuit Court of Appeals pursuant to 28 U.S.C. § 1292(b).

Memorandum of Decision and Order
dated April 15, 1983

The Motion to Reargue

Defendants seek to reargue the court's decision striking the jury demands. The briefs do nothing more than restate defendants' position in opposing plaintiff's motions. The motion to reargue is denied.

The Motion for Recusal

The claim of bias is based on the contact the undersigned had through a civil case brought by the Secretary of Labor to enjoin the trustees from making a loan in violation of Sections 404(a)(1)(B) and (C) of ERISA, 29 U.S.C. §§ 104(a)(1)(B) and (C), *Marshall* v. *Teamsters Local 282 Pension Trust Fund*, 458 F. Supp. 986 (E.D.N.Y. 1978) and a criminal proceeding in which the defendant John Cody was convicted of violation of 18 U.S.C. § 1962(c), 26 U.S.C. §§ 7201 and 7206(1) and 29 U.S.C. § 186(b)(1).[1]

The Court in *United States* v. *Bernstein*, 533 F.2d 775, 785 (2d Cir.), *cert. denied*, 429 U.S. 998, 97 S. Ct. 523 (1976) held:

> The rule of law without belaboring the point, is that what a judge learns in his judicial capacity—whether by way of guilty pleas of co-defendants or alleged co-conspirators, or by way of pretrial proceedings, or both—is a proper basis for judicial observations, and the use of such information is not the kind of matter that results in disqualification. Rules against "bias" and "partiality" can never mean to require the total absence of preconception, predispositions and other mental habits.

The court again had occasion to underscore the basis of disqualification as resting on personal bias stemming from extrajudicial sources in *United States* v. *Wolfson*, 558 F.2d 59, 62 (2d Cir. 1977):

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[1] The case is presently on appeal.

Memorandum of Decision and Order
dated April 15, 1983

> Both §§ 455(b)(1) and 144 refer to '*personal* bias' as triggering the requirement of recusal (emphasis supplied). And the cases construing both these sections have consistently held that for an alleged bias to be 'personal,' it 'must stem from an extrajudicial source . . . *United States* v. *Grinnell Corp.*, 384 U.S. 563, 583, 86 S. Ct. 1698, 1710, 16 L.Ed.2d 778 (1966) (interpreting § 144); accord with respect to § 455; *Davis* v. *Board of School Commissioners of Mobile County*, 517 F.1d [sic] 1044, 1051-52 (5th Cir. 1975), *cert. denied*, 425 U.S. 944, 96 S. Ct. 1685, 48 L.Ed.1d [sic] 188 (1976); *Lazofsky* v. *Sommerset Bus Co.*, 389 F. Supp. 1041, 1044-45 (E.D.N.Y. 1975).[2]

See also *United States* v. *Covens*, 662 F.2d 162, 167-69 (2d Cir. 1981), *cert. denied*, 456 U.S. 916, S. Ct. (1962); *In re IBM Corporation*, 618 F.2d 923, 929 (2d Cir. 1980); *In re Corrugated Container Antitrust Litigation*, 614 F.2d 958 (5th Cir. 1980).[3] The motion for recusal is denied.

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[2] 28 U.S.C. § 144 provides in pertinent part:

> Whenever a party to any proceeding in a district court makes and files a timely and sufficient affidavit that the judge before whom the matter is pending has a personal bias or prejudice either against him or in favor of any adverse party, such judge shall proceed no further therein, but another judge shall be assigned to hear such proceeding.

28 U.S.C. § 455 states in pertinent part:

> (a) Any judge . . . shall disqualify himself in any proceeding in which his impartiality might reasonable be questioned.
>
> (b) He shall also disqualify himself in the following circumstances:
>
> (1) Where he has a personal bias or prejudice concerning a party, or personal knowledge of disputed evidentiary facts concerning the proceeding.

[3] In *In re Corrugated Container*, *supra*, the judge had presided over a criminal trial in which the defendant in the subsequent

(footnote continued on following page)

Memorandum of Decision and Order
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Application for Certification Under 28 U.S. 1292(b)

We are aware that certification to review the right to trial by jury has been granted under § 1292(b) where the question presented on that issue involves a "question of law as to which there is substantial ground for difference of opinion." *See e.g., Pons* v. *Lorillard,* 549 F.2d 950, 951-52 (4th Cir. 1977), *aff'd,* 434 U.S. 575, 98 S. Ct. 866 (1978); *Zenith Radio Corp.* v. *Matsushita Elec. Indus. Co.,* 478 F. Supp. 889, 945-46 (E.D. Pa. 1979), we find no such doubt here.

The motion for certification under § 1292(b) is denied.

Defendants may bring their argument for review by the Court of Appeals by petitioning for a writ of mandamus. *See Lee Pharmaceuticals* v. *Mishler,* 526 F.2d 1115 (2d Cir. 1975).

The consolidated non-jury trial is scheduled to start on Monday, April 25, 1983 at 10:00 a.m. The trial is adjourned to Thursday, April 28, 1983 at 10:00 a.m. If the defendants file a petition for mandamus with the Clerk of the Second Circuit Court of Appeals on or before Friday, April 22, 1983, the trial will be stayed pending a determination of the matters raised in the petition provided defendants seek an expedited appeal and diligently prosecute the appeal.

So Ordered.

.....

U.S.D.J.

(footnote continued from previous page)

civil trial was acquitted. The judge expressed his opinion that the defendant was guilty. The Fifth Circuit Court of Appeals in affirming the judge's denial of recusal found that "all of the statements reflect comments on the evidence, and, at most, opinions developed through Judge Singleton's participation in the case. *Id.* at p. 967.

Memorandum of Decision and Order dated July 21, 1983

UNITED STATES DISTRICT COURT

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CV 81-2277

TED KATSAROS, et al.,

Plaintiffs,

—against—

JOHN CODY, et al.,

Defendants.

JOHN CODY, et al.,

Third-Party Plaintiffs,

—against—

ANTHONY G. ANGELOS, et al.,

Third-Party Defendants.

TEAMSTERS LOCAL 282 PENSION TRUST FUND,

Second Third-Party Plaintiff,

—against—

ANTHONY G. ANGELOS, et al.,

Second Third-Party Defendants.

Memorandum of Decision and Order
dated July 21, 1983

CV 82-1920

RAYMOND J. DONOVAN, Secretary of the United States Department of Labor,

Plaintiff,

—against—

JOHN CODY, et al.,

Defendants.

JOHN CODY, et al.,

Third-Party Plaintiffs,

—against—

ANTHONY G. ANGELOS, et al.,

Third-Party Defendants.

TEAMSTERS LOCAL 282 PENSION TRUST FUND,

Second Third-Party Plaintiff,

—against—

ANTHONY G. ANGELOS, et al.,

Second Third-Party Defendants.

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Memorandum of Decision and Order
dated July 21, 1983

MISHLER, *District Judge*

In February and March of 1979 the trustees of the Teamsters Local 282 Pension Trust Fund ("Trustees"), approved and disbursed a loan of $2 million to the Des Plaines Bankcorporation, Inc. ("Bankcorporation"), a bank holding company. The loan was secured by all the stock in the Des Plaines Bank ("Bank"), a wholly-owned subsidiary of Bankcorporation. Following the closing of the Bank by federal and state regulatory officials on March 14, 1981, two separate actions were brought against the Trustees alleging violation of fiduciary duties under the Employee Retirement Income Security Act of 1974 ("ERISA"), 29 U.S.C. § 1101, et seq. The Teamsters Local 282 Pension Trust Fund ("Fund") was joined as a defendant. These actions were consolidated for pre-trial matters and are referred to here as the Katsaros action (CV 81-2277) and the Donovan action (CV 82-1920). The Trustees and the Fund brought separate third-party actions against the named directions of Bankcorporation ("Directors").

The above consolidated actions were tried to the court without a jury pursuant to the memorandum of decision and order dated April 5, 1983. That decision also severed the third-party claims in both actions. The issues decided herein relate only to the claims of the plaintiffs against the defendants and the defense interposed in the original actions (statute of limitations in the Katsaros action). The court finds:

I. THE LOAN TO THE DES PLAINES BANKCORPORATION, INC.

In the fiscal year ending February 28, 1979, the Fund had assets of approximately $58 million. Approximately 80% of such assets were invested in stocks, bonds and commercial paper. (Exh. C.). Since approximately 1965, John Cody was a trustee of the Fund and also a trustee of the

Memorandum of Decision and Order dated July 21, 1983

Welfare Fund and Annuity Fund of Local 282 of the International Brotherhood of Teamsters.[1] During all pertinent times herein, Cody was the Administrator of the Pension, Welfare and Annuity Funds.[2]

Some time in the latter part of January 1978, Cody met Anthony G. Angelos, president and chairman of the board of directors of Bankcorporation at a social or union function. Angelos advised Cody that the Bank was seeking a loan. Cody suggested that Angelos have his lawyers make formal application to the Fund. On February 7, 1979, Jonathan T. Howe, a partner in the Chicago law firm of Jenner & Block, and a director and counsel to Bankcorporation, and counsel to the Bank, wrote to John Cody. The letter proposed a $2 million loan with interest at the Bank's floating prime rate, principal of $250,000 payable annually, the balance due four years from the date of the loan, to be secured by all the outstanding stock of the Bank. Howe requested the opportunity "to meet with you and your Board of Trustees at your forthcoming meeting on February 27, 1979." (Exh. 2A).

Cody met with Howe and Angelos on February 26. However, it was not until the next day, February 27, at the meeting of the Trustees, that Howe distributed financial statements of Bankcorporation and the Bank, i.e., con-

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[1] Cody has been president of Local 282 of the International Brotherhood of Teamsters since 1976.

[2] At a meeting on or about October 28, 1977, the Fund had agreed to loan one Hyman Green $20 million to finance the construction of a hotel and gambling casino. Pursuant to the terms of the agreement dated February 22, 1978, Green deposited $50,000 with the Fund for costs incurred with relation to the loan. The loan was enjoined by this court on August 11, 1978. *See Marshall* v. *Teamsters Local 282 Pension Trust Fund*, 458 F. Supp. 986 (E.D.N.Y. 1978). The Fund charged the sum of $73,437.77 as expenses. The *Katsaros* action seeks judgment directing the Trustees to reimburse the Fund in the amount of $23,473.57 on the first stated claim.

solidated financial statements of Bankcorporation and the Bank, as of December 31, 1978 (Exh. 5A), financial statement of the Bank as of December 31, 1978 (Exh. 5B), and a comparative schedule of assets of the Bank as of December 31, 1977, November 30, 1978 and December 31, 1978. (Exh. 5C). The three documents consisted of about 35 pages of figures and explanatory notes. The Trustees (other than Cody) who attended the meeting learned of the application for the first time at the meeting.[3]

Harvey Colton, a certified public accountant employed by the Fund since the early 1950's, attended the meeting. Colton disclaimed sufficient training to express an opinion on the soundness of the loan and testified that no one on the Fund's staff had sufficient training to express an opinion on the loan. (Tr. at 117, 120).

Howe and Angelos made a two hour presentation after distributing the documents to the Trustees. Howe "touched on the highlights of the statement." (Tr. at 126). He showed that the Bank increased its assets of $68,000 in 1977 to $278,000 in 1978 and that "was the bottom line." (Tr. at 127 (Colton testimony); *see* Tr. at 46-47 (Cody Testimony)). Thereupon, the Trustees present unanimously voted to approve the loan as modified as follows:

> The terms of the loan would be for a payment of $125,000 of principal together with accrued interest on a semi-annual installments [sic] over a period of four years with a baloon [sic] payment at the end of the loan period. The amount of interest shall be at 1% over the prime rate of the Chase Manhattan Bank of New York with a floor of 10% computed on the basis of an actual 365 day year, until maturity.

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[3] Defendant Nappi was not present at the February 27 meeting. Nappi attended the Trustees meeting of March 20 and voted in support of a motion to ratify the loan.

> After maturity or default, the note shall bear interest at a rate of 2% over the prime rate of 11% per annum whichever is greater.

Exh. 6A at 10, minutes of Board of Trustees Meeting, Feb. 27, 1979.[4]

Bankcorporation was to pay a loan organization fee of $10,000 plus all expenses incurred in making the loan. Angelos was to give his personal guarantee for the repayment of the loan,[5] to be secured by Angelos' interest in vacant land on Halstead Street in Chicago.

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[4] The actual loan agreement provided that:

> The Note shall be repaid over a four year period with seven semiannual installments in the amount of $125,000 of principal together with accrued interest, with the remaining balance of principal and accrued interest to be paid in a final installment due four years from the date of the Note. The Note shall bear interest from its date until maturity at the rate of one percent over the prime rate of the Chase Manhatten [sic] Bank of New York (said prime rate being defined for the purposes hereof as the lowest interest rate regularly charged from time to time by such bank on 90-day loans to borrowers of the highest credit rating. Any change in the Note rate shall, for the purposes hereof, be effective as of the date of announcement by such bank of a change in its prime rate) or ten (10) per cent, whichever is greater, computed on the basis of an actual day month, 365 day year, until maturity. After maturity whether by acceleration or otherwise the Note shall bear interest at the rate of two (2) percent over the prime rate of Chase Manhattan Bank or eleven (11) percent per annum, whichever is greater.

Exh. 7.

[5] Though defendants suggest that the idea of Angelos' personal guarantee originated in the discussion, it is significant to note that Angelos had prepared a financial statement showing his net worth of $3,227,481 as of November 30, 1978. The accountant preparing the report stated that verification of Angelos' investment assets was "by reference to quoted market values and appraisals." One of the assets was a 63% interest in a vacant plot of land (60,000 square feet) on Halstead Street in Chicago, then used as a parking lot. Angelos' interest was stated to be worth $1,386,000. (Exh. 5D).

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The Trustees present unanimously authorized Cody and defendant Ralph Guercia to make the loan. Cody and Guercia, accompanied by Herbert Ballin, the Fund's counsel, left the next day for Chicago. They retained one Sherman Carmell, Esq., a Chicago lawyer, as their local counsel, to advise them on the closing loan documents and the requirements of local law. During the period that Ballin and Carmell were reviewing the loan documents with Howe (representing Bankcorporation), Cody and Guercia visited the Bank in the company of Angelos and viewed the real estate on Halstead Street.

The loan closed on March 1, 1979 at the offices of Jenner & Block. The closing documents included a mortgage on Angelos' interest in the Halstead property as collateral for Angelos' guarantee and an opinion letter from Jenner & Block. The Trustees were not provided with a title report of the Halstead property. The opinion letter of counsel stated that there were no actions, suits or proceedings pending against the Bankcorporation or the Bank which would adversely affect the operations of the Bankcorporation or the Bank. The proceeds of the loan were disbursed as follows:

Central National Bank	$1,032,426
South Side Bank	16,073
Water Tower Trust & Savings Bank	155,128
Anthony Angelos	288,373
Fund (loan organization fee)	10,000
Bankcorporation	500,000

(Exh. 12).

At a regular meeting of the Trustees on March 20, 1979, the Trustees (with Nappi present), unanimously ratified all the terms and conditions of the loan agreement and the actions of Cody and Guercia with reference to the loan.

The Fund received the first semi-annual installment of principal and interest in the amount of $253,548 (principal

in the amount of $125,000 and the balance as interest) on September 4, 1979 (due September 1, 1979). The Fund received two additional payments of principal and interest: $276,511 on February 28, 1980 (due March 1, 1980) and $228,374 on August 30, 1980 (due September 1, 1980).[6]

The loan agreement obligated Bankcorporation to submit financial statements to the lender on the then current condition of the borrower (i.e., Bankcorporation). The statements submitted were, however, incomplete.[7] Although circulated among the Trustees, these statements were unaccompanied by any report or analysis. A cursory examination of the documents would have revealed that the Bank had discussed corrective measures with the Federal Deposit Insurance Corporation ("FDIC") relating to the financial soundness of the Bank. The Trustees had the right to additional information and the right to demand additional security under the terms of the loan agreement, as in effect during the period March 1, 1979 to March 1, 1981.[8]

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[6] Interest was erroneously computed on the basis of the prime rate in effect one month prior to the due date on each semi-annual payment. Plaintiffs claim that failing to compute interest as provided in the loan agreement, i.e., the primate rate as it fluctuates on a "floating" basis, cost the fund approximately $32,500 in lost interest.

[7] For the period March 1979-March 1981, the Fund received: a one-page statement of condition of Bankcorporation, dated December 13, 1979; a set of audited financial statements for the Bank and Bankcorporation for the year 1979; a six-month unaudited, consolidated financial statement for the Bank and Bankcorporation, as of June 30, 1980; and an updated financial statement for Anthony G. Angelos, dated August 31, 1979. (Exh. 16A-E).

[8] In pertinent part, the loan agreement provides:

> 5.3 *Furnishing of Financial Statements and Information.* Borrower will maintain a modern system of accounting administered in accordance with generally accepted accounting

(footnote continued on following page)

Memorandum of Decision and Order
dated July 21, 1983

The Trustees' Fiduciary Duty Under
Section 404(a)(1)(B) of ERISA

The obligation of trustees of an employee benefit plan in investing a plan's assets is analyzed under common

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(footnote continued from previous page)

principles consistently maintaned [sic] and will deliver or cause to be delivered to Lender, in duplicate:

5.3.1 As soon as practicable and in any event within forty-five (45) days after the end of each accounting, quarterly financial statements of Borrower and Des Plaines Bank as of the end of such period including an income statement, balance sheet and surplus statement, setting forth in each case in comparative form figures for the corresponding period in the previous fiscal year (to the extent comparative figures are available) all in reasonable detail. To fairly present the financial condition of Des Plaines Bank and the Borrower as of the balance sheet date and the results of their operations for the period shown.

5.3.2 Within the 135 days after the end of the fiscal year of Borrower and the Des Plaines Bank, a copy of signed corporate financial statements, a copy of the annual audit report, prepared in conformity with generally accepted accounting principles applied on a basis consistent with that of the preceding fiscal year, and signed by independent certified public accountants satisfactory to Lender and a copy of the annual report, if any, to shareholders of the Des Plaines Bank.

5.3.3 Within reasonable promptness, such other data and information as from time to time may be reasonably requested by Lender.

5.3.4 Borrower will cause its outside auditors to furnish to Lender periodically and not less than semi-annually a certification that they are not aware of any event of default of any of the terms of this Agreement, or, if they are aware of such an event, its nature and extent.

5.4 *Inspection.* Borrower will permit and will cause the Des Plaines Bank to permit any authorized representative designated by Lender in writing to examine the books and records of Borrower and the Des Plaines Bank and take memoranda and extracts therefrom, as permitted by law.

. . . .

(footnote continued on following page)

law principles of trusts "bearing in mind the special nature and purpose of employee benefit plans." S. Rep. No. 1090, 93d Cong., 2d Sess. 302 (1974), *discussed in Marshall* v. *Teamsters Local 282 Trust Fund*, 458 F. Supp. 986, 990 (E.D.N.Y. 1978). *See also Donovan* v. *Daugherty*, 550 F. Supp. 390, 403 (S.D. Ala. 1982); *Marshall* v. *Glass/Metal Ass'n and Glaziers and Glassworkers Pension Plan*, 507 F. Supp. 378, 383 (D. Hawaii 1980); Note, *Fiduciary Standards and the Prudent Man Rule Under the Employment Retirement Income Security Act of 1974*, 88 Harv. L. Rev. 960, 966-67 (1975) [hereinafter *Fiduciary Standards*].

Section 404(a)(1)(B) of ERISA, 29 U.S.C. § 1104(a)(1)(B), defines the obligation of a trustee in investing the plan's assets under the "prudent man standard" as follows:

> [A] fiduciary shall discharge his duties with respect to a plan solely in the interest of the participants and beneficiaries and—
>
> . . . .

(footnote continued from previous page)

5.6 *Book Value of Collateral.* The stock of the Des Plaines Bank pledged as collateral hereunder shall at all times have a book value of no less than $2,000,000 determined in accordance with generally accepted accounting principles, provided however that only one-half of the reserves shall be used in the computation. In the event that the book value as determined shall at any time or times be less than the required amount, Borrowers will deliver or cause to be delivered additional shares of the Des Plaines Bank, or other acceptable securities or negotiable instruments duly endorsed as additional collateral in an amount sufficient to maintain said requirement.

5.7 *Insurance.* Borrower will cause the Des Plaines Bank to maintain insurance for the Des Plaines Bank to such extent and against such hazards and liabilities as is commonly maintained by companies similarly situated and will furnish upon request a statement showing details of the insurance being so maintained.

(B) with the care, skill, prudence, and diligence under the circumstances then prevailing that a prudent man acting in a like capacity and familiar with such matters would use in the conduct of an enterprise of a like character and with like aims.

Defendants argue that the evidence fails to support the alleged breach of fiduciary duty in that it shows that the Trustees relied in good faith on the presentation made by Angelos and Howe at the February 27 meeting.[9] They point to the consolidated financial statement (Exh. 5A) which showed an increase in assets from $42 million to $52 million during the year 1978. The financial statements showed the income to Bankcorporation from the Bank increased to $427,110 in 1978 from $186,959 in 1977; the statements showed the loss reserve increased in 1978 to $246,336, from $220,000 in 1977, while the actual loan losses decreased from $126,707 in 1977 to $82,261 in 1978. (Exh. 5A)

Defendants further argue that (employer-trustee) Herbert Schneider's insistence on Angelos' personal guarantee, collateralized as indicated, showed a measure of good business judgment and prudence in considering the loan.

The duties of a trustee are "the highest known to the law." *Donovan* v. *Bierwirth*, 680 F.2d 263, 272 n.8 (2d Cir.), *cert. denied*, —— U.S. ——, 103 S. Ct. 488 (1982). *See Restatement (Second) of Trusts* § 2 comment b (1959) ("The duties of a trustee are more intensive than the duties of some other fiduciaries.") The prudent man standard of care is the objective

[9] The Trustees were advised that Angelos had some experience in banks prior to acquiring an interest in Bankcorporation in 1977; he had been considered for appointment to the position of Commissioner of Insurance for the State of Illinois. Howe was a member of the prestigious law firm of Jenner & Block in Chicago.

> standard of a man of ordinary prudence in dealing with his own property. A trustee is liable for a loss resulting from his failure to use the care and skill of a man of ordinary prudence, although he may have exercised all the care and skill of which he was capable.

Restatement (Second) of Trusts § 174 comment a (1959). *See* Bogert, *Trusts & Trustees* § 541, at 164 (rev. 2d ed. 1978).

Where a trustee does not possess the education, experience and skill required to make a decision concerning the investment of a plan's assets, he has an affirmative duty to seek independent counsel in making the decision. *Donovan* v. *Bierwirth*, 680 F.2d at 272-73, *Donovan* v. *Bierwirth*, 538 F. Supp. 463, 470 (E.D.N.Y. 1981), *aff'd as modified*, 680 F.2d 263 (2d Cir.), *cert. denied*, —— U.S. ——, 103 S. Ct. 488 (1982), *citing Fiduciary Standards*, *supra* at 965; *Mills* v. *Bluestein*, 275 N.Y. 317 (1937); *Chemical Bank & Trust Co.* v. *Reynaud*, 150 Misc. 821, 270 N.Y.S. 301 (Sup. Ct.), *aff'd*, 239 A.D. 904, 265 N.Y.S. 944 (1st Dep't 1933). The failure to seek outside counsel when "under the circumstances then prevailing . . . a prudent man acting in a like capacity and familiar with such matters" would seek outside counsel, is imprudent and a violation of ERISA. Section 404(a)(1)(B) of ERISA, 29 U.S.C. § 1104(a)(1)(B). The conduct of a trustee in making an independent investigation is an indication of the care and diligence of the trustee in arriving at an investment decision. A trustee unfamiliar with an unusual or difficult investment decision is charged with making an "independent inquiry into the merits of particular investments rather than [relying] wholly upon the advice of others." *Withers* v. *Teachers' Retirement System*, 447 F. Supp. 1248, 1254 (S.D.N.Y. 1978), *aff'd mem.*, 595 F.2d 1210 (2d Cir. 1979); *see* Bogert, *supra*, § 541, at 164-65.

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A trustee's duty to make an independent investigation includes the negative obligation of not relying on the representations, predictions and hopes of a borrower.

Relying on the advice or information of a co-trustee alone may subject a trustee to liability. If a trustee believes that a co-trustee is violating his fiduciary obligation, he must make "reasonable efforts under the circumstances to remedy the breach." Section 405(a)(3) of ERISA, 29 U.S.C. § 1105(a)(3). *See Morrissey* v. *Curran*, 567 F.2d 546, 549-51 (2d Cir. 1977) (Lumbard, J., concurring).

Here, the manner in which the loan to Bankcorporation was proposed and presented was designed to discourage inquiry into the merits. Urgency and speed overrode the need for calm deliberate inquiry and discussion.[10] Colton apparently attended the meeting to advise the Board members on other matters on the agenda. No Trustee asked him to express his opinion on the advisability of making the loan. At any rate, he did not think that he was qualified to express an opinion with relation to the financial statements of Bankcorporation and the Bank. (Tr. at 114-25). The Trustees considered only the information and representations given by the borrowers, as presented by Angelos and Howe.

An independent investigation would have disclosed that it would have been imprudent to make the loan based on the financial statements of Bankcorporation and the Bank. The sole source of income of Bankcorporation was the earnings of the Bank. An analysis of the financial statements by an expert would have revealed the following:

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[10] Cody had not even discussed the loan with Harvey Colton, the Plan's accountant, prior to the meeting. See Tr. at 115-16 (Colton's testimony).

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Capital Adequacy

The net worth of Bankcorporation and the Bank as set forth in the financial statement submitted to the Trustees on February 27 was $1.8 million. This included an item of goodwill valued at $1.3 million. The tangible net worth of Bankcorporation was only $500,000. Since this net equity figure is based on the quality of the loans the Bank made (as part of the Bank's assets), an analysis of the loans would have been part of the investigation. The significant increase in earnings for the year 1978 over 1977 would indicate that the Bank's loans were at a higher than normal interest rate and therefore riskier. The increase in the Bank's loans, though generating more income, placed the limited resources of the Bank in greater danger of loss.[11] The ratio of the Bank's equity (net worth) to its loans and other assets as of December 31, 1978 was 4.53%. In the State of Illinois, comparing the capital adequacy of the Bank with other banks of similar size, the Bank ranked 149th out of 151 banks. (Exh. 28, 28A).

Loan Loss Reserve

Despite the substantial increase in loans the Bank's loan loss reserve was increased to only $246,334 as of December 31, 1978, from $220,000 as of December 31, 1977. The percentage of the loss reserve to outstanding loans fell from 1.03% to .75%. A conservative estimate of loan loss reserve would be 1% of the outstanding loans. The loan loss reserve should have been not less than $327,000. The decrease in percentage was a factor in showing higher net earnings for the year 1978.

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[11] The aggregate amount of loans made by the Bank as of December 31, 1977 was $21 million. On December 31, 1978 it was $32.7 million, an increase of 55%.

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Profitability

The Bank earned .76% on its assets in 1977. The statements reported an increase to .94% in 1978. The earning power of a bank is measured by the ratio of earnings to total assets. The earning power of the Bank was ranked 96th out of 151 banks of comparable size in Illinois. The statistics do not reflect the interest on the loan as a charge against the bank since the loan was the obligation of Bankcorporation. If such charge were made, the earning power would, consequently, be reduced proportionately. (Exh. 28).

Ability to Repay

The loan agreement required payments of principal in the amount of $250,000 plus interest in the amount of approximately $200,000 in 1980 and 1981 (interest of approximately $130,000 in 1982). The net income of Bankcorporation in 1978 was $278,000. Bankcorporation would be unable to meet the loan obligations from its net income, if the earnings were at the 1978 level, even based on the favorable method of stating its earnings.

Liquidity

The Trustees were advised that the Bank had a cash flow problem. The increase of $500,000 in the available cash could only have a minimum effect toward solution of the problem. The total deposits of the Bank increased 24% in 1978. The Bank's total loans constituted a sum equal to 67% of its deposits. If the deposits were withdrawn at a faster rate than the loans were repaid, the Bank could have been embarrased. An inquiry into the nature of the increased deposits was appropriate.

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The Bank Stock as Security

The financial statement of the Bank valued the stockholders' equity at $2 million as of December 31, 1978. Acceptance of this figure as the value of the security was imprudent. Ordinarily, the value of bank stock to a lender who is not in the banking business is highly uncertain. On default, the Trustees would have found it difficult to sell the stock to multi-bank holding corporations under Illinois law. Based on the financial statement, the Bank's stock was inadequate security for the loan.

Angelos' Guarantee

1. *Appraisal*

Angelos' personal guarantee was secured by his interest in vacant land (used as a parking lot) on Halstead Street near downtown Chicago. Angelos' statement of assets valued the land at $2.8 million subject only to "loan and sundry advances" in the amount of $600,000. It also stated that "[t]he valuations contained herein are based on appraisals." The statement showed Angelos' interest to be 63% and the value of his interest to be $1,386,000.

The Trustees failed to order an independent appraisal of the property; they did not request the appraisal on which Angelos based the value of $1,386,000, as stated in his financial statement. After the default by Bankcorporation in the payments due under the loan in March 1981, the Trustees had the property appraised. It was appraised at $1 million. Based on this appraisal, Angelos' interest in the property should have been valued at about $252,000 and not $1,386,000. Such an inquiry would probably have led the Trustees to question the value of other assets in the financial statement.

2. *Title*

On March 1, 1979, the very day of the loan closing in Chicago, the Halstead Street property was sold by Cook County for unpaid general taxes for the year 1977. The Trustees failed to have a title (and tax) search, which would have revealed a default in the payment of taxes for the years 1977 and 1978 (approximately $2,000). The property was redeemed by Angelos on September 7, 1979.[12]

Inquiry of Des Plaines Bank's Lender

With a minimum of effort the Trustees could have questioned the Central National Bank concerning the history of its loan to the Bank. The unpaid principal amount of the loan at that time was about $1 million and renewal of the loan was refused by Central National. In all probability, inquiry would have led the Trustees to learn that at least five (5) banks in the Chicago area refused to refinance the Central National Bank loan which was due to mature on March 1, 1979. Such inquiry could reasonably have led to a disturbing report issued by the FDIC underscoring the Bank's undercapitalization, its loan-deposit ratio, and the high percentage of both substandard loans and restaurant loans.

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[12] The retention of counsel to inquire into questions of title does not relieve the trustee of his duty to investigate.

> While the taking of *advice of counsel* or other specialist has some effect in tending to show the use of reasonable care by a trustee, it is not conclusive. The trustee has a duty to examine the opinion of the specialist so far as the ability of a reasonably intelligent man would permit and to exercise what judgment he can as to its soundness. Thus if it is a valuation by a real estate appraiser the trustee may well require that the elements of value be separately stated. . . . The trustee cannot shift the burden of decision to others.

Bogert, *supra*, § 541 at 164-65 (emphasis in original) (fotnotes [sic] omitted).

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Conclusion

In approving the loan of $2 million to Bankcorporation the Trustees violated their fiduciary obligation to the participants and beneficiaries of the Fund under Section 404(a)(1)(B) of ERISA, 29 U.S.C. § 1104(a)(1)(B), by failing to use that degree of care, skill, prudence and diligence that a prudent man would exercise under the circumstances then prevailing. Defendant Nappi, having voted on March 20, 1979 to ratify and approve the loan, in violation of his duty to disapprove, is jointly liable with the other Trustees for any loss to the Fund.

II. The Expenses Respecting a Loan to Hyman Green

The Katsaros complaint (in addition to seeking relief based on the imprudent loan made to Bankcorporation), seeks reimbursement of expenses in connection with the agreement to loan one Hyman Green $20 million to finance the construction of a hotel and gambling casino in Las Vegas, Nevada. This court enjoined the loan to Green as violative of Section 404(a)(1) of ERISA, 29 U.S.C. § 1104(a)(1). *Marshall* v. *Teamsters Local 282 Pension Trust Fund,* 458 F. Supp. 986 (E.D.N.Y. 1978). The agreement required Green to pay all costs and expenses related to the loan. Katsaros alleges that the Fund expended sums in excess of $100,000. The Trustees state that the sum of $73,473.57 was disbursed; that Green reimbursed the Fund in the amount of $50,000 and the balance of $23,474.57 is due and owing from Green. The Trustees assert the statute of limitations under Section 413 of ERISA, 29 U.S.C. § 1113 as a bar.[13]

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[13] Section 413 of ERISA, 29 U.S.C. § 1113, provides:

§ 1113. Limitation of actions.

[(a)] No action may be commenced under this title with respect to a fiduciary's breach of any responsibility, duty,

(footnote continued on following page)

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The parties stipulated to agreement on the following facts:

1. The Green loan agreement was signed in February 1978.

2. Katsaros and other named plaintiffs knew of the loan agreement prior to March 23, 1978.

3. The Secretary of Labor instituted the action entitled *Marshall* v. *Teamsters Local 282 Pension Trust Fund* by filing a complaint with the Clerk of the Court on April 23, 1978.

4. Katsaros and other named plaintiffs were aware of the pendency of the *Marshall* action prior to March 31, 1978.

6. By memorandum of decision and order dated August 11, 1978, after a trial on the merits, this court held that the loan agreement violated Section 404(a)(1)(B)-(C) of ERISA, 29 U.S.C. § 1104(a)(1)(B)-(C), and directed the

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(footnote continued from previous page)

> or obligation under this part, or with respect to a violation of this part, after the earlier of—
>
> > (1) six years after (A) the date of the last action which constituted a part of the breach or violation, or (B) in the case of an omission, the latest date on which the fiduciary could have cured the breach or violation, or
> >
> > (2) three years after the earliest date (A) on which the plaintiff had actual knowledge of the breach or violation, or (B) on which a report from which he could reasonably be expected to have obtained knowledge of such breach or violation was filed with the Secretary under this title;
>
> except that in the case of fraud or concealment, such action may be commenced not later than six years after the date of discovery of such breach or violation.

entry of judgment enjoining the Trustees from performing the terms of the loan agreement. 458 F. Supp. at 986.

7. Green brought an action against the Fund and the Trustees on November 5, 1980, *Green* v. *Teamsters Local 282 Pension Trust Fund, et al.,* No. CV 80-3077, to recover certain expenses. On March 16, 1981, the Fund interposed an answer in that action including a counterclaim for the unpaid balance of the sums disbursed in the amount of $23,473.57.

8. Green filed his reply to the counterclaim on April 1, 1981.

9. Plaintiffs were unaware that reimbursement had not been made in full by Green until the Fund interposed its counterclaim.

10. The *Katsaros* action was commenced on July 14, 1981.

The *Katsaros* action is brought by Katsaros, Kuebler, Trott, Kudla and Curd as participants in the Fund pursuant to Section 502(a)(3) of ERISA, 29 U.S.C. § 1132(a)(3) for reimbursement of monies spent in "arranging the aforedescribed prohibited transaction and unsuccessfully defending the aforedescribed injunctive action . . . ." (Par. 10, Amended Complaint). The court is presented with the question as to when plaintiffs "had actual knowledge of the breach or violation."

Plaintiffs were aware, or should have been aware, of the Trustees' violation of their fiduciary duty (in agreeing to make the loan to Green) at the time the claim of the Secretary was pending in *Marshall* v. *Teamsters Local 282 Pension Fund, supra.* Katsaros fixes the date prior to March 31, 1978. *Arneil* v. *Ramsey,* 550 F.2d 774, 780 (2d Cir. 1977); *Berry Petroleum Co.* v. *Adams & Peck,*

518 F.2d 402, 410 (2d Cir. 1975). However, the breach of fiduciary duty claimed here is based on the failure of the Trustees to take the necessary steps to recover monies expended with relation to the Green loan, including the expenses of defending the action brought by the Secretary. Costs and disbursements in defense of that action could not be determined before August 11, 1978 when the court filed its memorandum of decision and order. The obligation of the Trustees to demand reimbursement was a continuing one. The court finds (on the stipulation of facts) that the Trustees did not make their demand of Green until they interposed a counterclaim on March 16, 1981.

I find the *Katsaros* action was timely brought on March 14, 1981; within three (3) years of this Court's decision and order of August 11, 1978. Three years is the shortest period of limitation set forth under 29 U.S.C. § 1113.[14] Thus, under any method of analysis, the Trustees' defense under the ERISA statute of limitations must be rejected.

III. Conclusion

Plaintiffs in *Donovan* v. *Cody,* CV 82-1920, and *Katsaros* v. *Cody,* CV 81-2277, are entitled to judgment against the defendant Trustees directing the defendants jointly and severally for any and all loss resulting from the default by Bankcorporation in the terms and conditions of the loan agreement.

Plaintiffs in *Katsaros* v. *Cody* are entitled to judgment against the defendant Trustees (except Guercia) directing such defendants to pay the sum of $23,473.57, together with interest from the day the monies were disbursed.

The case is set down for a hearing on August 19, 1983 at 1:00 p.m. to determine damages in addition to those

[14] *See* note 13, *supra.*

above mentioned resulting from the default in the loan agreement and any other relief to which the plaintiffs are entitled as a result of the Trustee's violation of their fiduciary duty.

So ORDERED.

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U. S. D. J.

Memorandum of Decision and Order dated August 18, 1983

UNITED STATES DISTRICT COURT

EASTERN DISTRICT OF NEW YORK

CV 81-2277

TED KATSAROS, et al.,

Plaintiffs,

—against—

JOHN CODY, et al.,

Defendants.

JOHN CODY, et al.,

Third-Party Plaintiffs,

—against—

ANTHONY G. ANGELOS, et al.,

Third-Party Defendants.

TEAMSTERS LOCAL 282 PENSION TRUST FUND,

Second Third-Party Plaintiff,

—against—

ANTHONY G. ANGELOS, et al.,

Second Third-Party Defendants.

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CV 82-1920

RAYMOND J. DONOVAN, Secretary of the United States Department of Labor,

Plaintiff,

—against—

JOHN CODY, et al.,

Defendants.

JOHN CODY, et al.,

Third-Party Plaintiffs,

—against—

ANTHONY G. ANGELOS, et al.,

Third-Party Defendants.

TEAMSTERS LOCAL 282 PENSION TRUST FUND,

Second Third-Party Plaintiff,

—against—

ANTHONY G. ANGELOS, et al.,

Second Third-Party Defendants.

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Memorandum of Decision and Order
dated August 18, 1983

MISHLER, *District Judge*

In February and March of 1979 the trustees of the Teamsters Local 282 Pension Trust Fund ("Trustees"), approved and disbursed a loan of $2 million to the Des Plains [sic] Bankcorporation, Inc. ("Bankcorporation"), a bank holding company. The loan was secured by all the stock in the Des Plains [sic] Bank ("Bank"), a wholly-owned subsidiary of Bankcorporation. Following the closing of the Bank by federal and state (Illinois) regulatory officials on March 14, 1981, two separate actions were brought against the Trustees alleging violations of fiduciary duties under the Employee Retirement Income Security Act of 1974 "(ERISA"), 29 U.S.C. § 1101, *et seq.* The Teamsters Local 282 Pension Trust Fund ("Fund") was joined as a defendant. These actions, which were consolidated for pre-trial matters, are referred to here as the Katsaros action (CV 81-2277) and the Donovan action (CV 82-1920). The Trustees and the Fund have brought separate third-party actions against the named directors of Bankcorporation ("Directors"). The Fund's actions also join Jenner & Block (counsel to Bankcorporation) as a third-party defendant.

By decision dated April 5, 1983 this court consolidated the main actions for trial and severed the third-party claims in both actions. Subsequently, by Memorandum of Decision and Order dated July 21, 1983, the court found the Trustees liable for violation of their fiduciary duties under ERISA. Familiarity with the record is assumed for the purposes of this decision.

Before us now are motions brought by certain third-party defendants seeking to dismiss the claims raised against them by the two first-party plaintiffs, *i.e.*, the Trustees and the Fund. Additionally, third-party defendant Anthony G. Angelos seeks to vacate the notice of default entered against him.

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Memorandum of Decision and Order
dated August 18, 1983

I. The Third-Party Complaints

Briefly stated, the third-party plaintiffs raise claims under the federal securities statutes and ERISA as well as common law claims of fraud respecting the $2 million loan described above. The Trustees' third-party complaint in the Katsaros action is identical with that filed by the Trustees in the Donovan action. The third-party complaints filed by the Fund (as amended) differ from those filed by the Trustees in two respects, *i.e.*, the Fund has (1) joined Jenner & Block and (2) charged all third-party defendants with violating certain provisions of ERISA. All third-party complaints allege the following:

In the summer of 1978 Central National Bank in Chicago ("CNB") advised the Bank that it would not renew an outstanding loan in the amount of $1,500,000 which was due on August 31, 1978. Subsequently, CNB granted the Bank a number of extensions and finally, in February, 1979, advised the Bank that payment of the indebtedness would be required on or before March 1, 1979.

Anthony G. Angelos, one of the Directors, telephoned the Fund from Chicago to inquire whether the Fund would consider lending $2 million to the Bank. On February 27, 1979 Angelos and Jonathan T. Howe, Director and Counsel to Bankcorporation, came to the Fund's office in Elmont, New York and made a presentation to the Trustees, urging that the loan be made before March 1, 1979. On the following day, two Trustees, Cody and Guercia, travelled to Chicago to examine the bank and the proposed real estate collateral with a view to making the loan.

The third-party complaints claim that Angelos and Howe concealed the true financial condition of the Bank. At the time the loan was proposed to the Fund, Angelos, Howe, Jensen and Kirie allegedly were aware that the Federal

Memorandum of Decision and Order
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Deposit Insurance Corporation (FDIC) had completed a semi-annual investigation of the Bank and found serious "Unacceptable and Objectionable Conditions and or Practices." The third-party plaintiffs charge that the concealments and misrepresentations were made with either "the intent to defraud the Fund and the Trustees with reckless disregard of the truth thereof or negligently." Complaints ¶ 18.

The loan was made on March 1, 1979 in reliance upon the allegedly false representations. As part of the security for the loan, the Bank pledged 68,267 shares of its stock (at least 95% of the shares of stock issued).

All third-party complaints charge violations of § 17(a) of the Securities Act of 1933, 15 U.S.C. § 77q(a); § 10(b) of the Exchange Act, 15 U.S.C. § 78j(b) and Rule 10b-5, 17 C.F.R. § 240.10b-5; as well as common law fraud and negligence. Additionally, the Fund charges that the third-party defendants "knowingly participated in the alleged breach of the Trustees' fiduciary duty" and thus violated § 404(a)(1)(A) and (B) of ERISA, 29 U.S.C. § 1104(a)(1)(A) and (B). Both third-party complaints in both actions seek indemnity for all sums recovered from the Trustees in the original action.

II. Motions to Dismiss the Third-Party Complaints

Certain third-party defendants bring motions to dismiss the third-party complaints.[1] Briefly stated, the Fund's

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[1] Third-party defendants Jonathan T. Howe, James C. Kirie, Clarence L. Jensen and Lambrose Karkazis seek (1) dismissal of the federal securities claims pursuant to Rule 12(b)(6), Fed.R. Civ.P.; (2) dismissal of fraud claims pursuant to Rules 9(b) and 12(b)(2) and (5), Fed.R.Civ.P., and (3) dismissal of the misrepresentation claim pursuant to Rule 12(b)(2)(5) and (6). In addition, Howe seeks dismissal of the fraud and misrepresentation

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third-party complaint is challenged under Rule 14(a), Fed.R.Civ.P., on the grounds that third-party impleader is improperly sought here. The Fund's ERISA claim is challenged (1) under Rule 12(b)(6), Fed.R.Civ.P., on the grounds that the allegations fail to state a claim under ERISA upon which relief can be granted, and (2) under Rule 12(b)(1), Fed.R.Civ.P., on the grounds that the jurisdiction of this court over civil actions under ERISA does not encompass actions brought by the Fund. *See* ERISA § 502(e)(1), 29 U.S.C. § 1132(e)(i).

The Trustees' federal securities claims are challenged under Rule 12(b)(6) on the grounds that in the absence of a "sale" of securities to the Trustees, the allegations fail to state a claim upon which relief can be granted. The fraud and misrepresentation claims are challenged under Rule 12(b)(6), Fed.R.Civ.P., and the fraud claims are also challenged as to sufficient specificity under Rule 9(b), Fed.R.Civ.P. Additionally, challenges are raised as to the court's subject matter jurisdiction over the controversy and the court's personal jurisdiction over the defendants.

For the reasons set forth below, this court (1) dismisses in all respects the third-party complaints filed by the Fund; (2) dismisses the federal securities claims brought by the

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claims pursuant to 12(b)(4) and Kirie, Jensen and Karkazis move to dismiss the fraud claim pursuant to Rule 12(b)(6).

The third-party defendant law firm, Jenner & Block, seeks dismissal of the Fund's federal securities claims, ERISA claims, and fraud and misrepresentation claims pursuant to Rule 12(b)(2) and (6), Fed.R.Civ.P. Additionally, the fraud and misrepresentation claims are challenged under Rule 14(a), Fed.R.Civ.P.

All motions to dismiss challenge the Fund's third-party action under Rule 14(a), Fed.R.Civ.P. The ERISA claim set forth by the Fund is challenged under Rule 12(b)(1) and 12(b)(6), Fed. R.Civ.P.

Third-party defendants C. J. Bassler, James Kokonas, James Verros and Herbert Wenske were never served.

Trustees; (3) grants the Trustees leave to replead fraud claims with respect to certain defendants; and (4) invites the parties to address the proposed transfer of the Trustees' third-party actions to the United States District Court for the Northern District of Illinois pursuant to 28 U.S.C. § 1404(a).

III. Third-Party Action Brought by the Fund

Plaintiffs in the main actions do not seek to impose liability on the Fund. The amended Katsaros and Donovan complaints joined the Fund as a nominal party defendant. Although relief respecting damage was available to plaintiffs without such joinder, it was "desirable to join" the Fund as a party since judgment (if plaintiffs are successful) will affect the composition of the Trustees of the Fund. *See Provident Tradesmens Bank & Trust Co.* v. *Patterson*, 390 U.S. 102, 110, 88 S. Ct. 733, 738 (1968).

We find that the Fund's third-party complaints improperly seek indemnification. A third-party complaint may be served on a non-party "who is or may be liable to him for all or part of the plaintiff's claim against him." Rule 14(a). The main actions herein were brought for the benefit of the Fund. Thus, the Fund "stands in the same position as the original plaintiff[s]. In this situation the third-party defendant's liability is not the secondary or derivative liability required for impleader." *U. S. General, Inc.* v. *City of Joliet*, 598 F.2d 1050, 1053 (7th Cir. 1979); *Commodity Futures Trading Comm'n* v. *Hunt*, 591 F.2d 1211, 1224 (7th Cir.), *cert. denied*, 442 U.S. 921, 99 S. Ct. 2848, *reh'g denied*, 444 U.S. 888, 100 S. Ct. 189 (1979); *McCain* v. *Clearview Dodge Sales, Inc.*, 574 F.2d 848, 849-50 (5th Cir. 1978); *House* v. *Mine Safety Appliances Co.*, 573 F.2d 609, 622 (9th Cir.), *cert. denied*, 439 U.S. 862, 99 S. Ct. 182 (1978).

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The Fund's third-party complaints herein are inaccurately based upon notions of derivative liability and are, accordingly, dismissed pursuant to Rule 12(b)(6), Fed.R. Civ.P. Any claim the Fund may have under the federal securities laws[2] may be asserted in an independent action. Because we dismiss the Fund's third-party complaints in all respects, we need not address the Fund's claims regarding (1) common law fraud and misrepresentation or (2) participation in the Trustees' breach of fiduciary duty in violation of ERISA.

Jenner & Block is joined by the Fund but not by the Trustees. As a result of our dismissal of the Fund's third-party complaints, all charges against Jenner & Block are dismissed.

IV. Third-Party Action Brought by the Trustees

A. *Violation of Securities Statutes (First and Second Claims)*

In the matter before us, the subject securities were the shares of stock in the Bank which were pledged to the Fund by Bankcorporation as security for the loan. The Trustees were not buyers, sellers or pledgees of such securities. The First and Second Claims asserted by the Trustees are therefore insufficient as a matter of law. *Blue Chip Stamps* v. *Manor Drug Stores,* 421 U.S. 723, 731-36, 95 S. Ct. 1917, 1923-25, (1975), citing *Birnbaum*

[2] Unlike the Trustees, the Fund may assert claims under the federal securities statutes. The United States Court of Appeals for the Second Circuit has held that a pledge of stock constitutes a "sale" for purposes of the federal securities law. *Mallis* v. *F.D.I.C.,* 568 F.2d 824 (2d Cir. 1977), *cert. dismissed, sub nom; Bankers Trust Co.* v. *Mallis,* 435 U.S. 381, 98 S. Ct. 1117 (1978); *United States* v. *Gentile,* 530 F.2d 461 (2d Cir.), *cert. denied,* 426 U.S. 936, 96 S. Ct. 2651 (1976). Thus, the Fund, as pledgee of the Bank stock has standing to sue under securities statutes.

v. *Newport Steel Corp.*, 193 F.2d 461, 463-4 (2d Cir.), *cert. denied*, 343 U.S. 956, 72 S. Ct. 1051 (1952).

The First and Second claims are dismissed as to all third-party defendants pursuant to Rule 12(b)(6). As a result, provisions of the Securities Act of 1933 and the Securities Exchange Act respecting nationwide jurisdiction for actions involving violations of such statutes are inapplicable herein. *See* Securities Act of 1933, § 22(a), 15 U.S.C. § 77v(a) (1975), Securities Exchange Act of 1934, § 27, 15 U.S.C. § 78aa (1976).

B. *Subject Matter Jurisdiction*

The Trustees, all residents of New York, bring this third-party action alleging that all the Directors "are citizens of a state other than the State of New York" (Complaints ¶ 11). Thus, following our dismissal of claims brought under the federal securities statutes, the jurisdiction of this court over the subject matter of the Trustees' common law claims of fraud and misrepresentation is based upon diversity of citizenship, pursuant to 28 U.S.C. § 1332. Accordingly, motions to dismiss pursuant to Rule 12(b)(1) are denied.

C. *Venue*

The venue of these actions is not challenged by the third-party defendants. The federal venue statute, 28 U.S.C. § 1391(a) provides:

> A civil action wherein jurisdiction is founded only on diversity of citizenship may, except as otherwise provided by law, be brought only in the judicial district where all plaintiffs or all defendants reside, or in which the claim arose.

We find that venue is properly laid in New York where all the plaintiffs reside. Where, as here, venue is properly

laid, a district court may, nonetheless, transfer the action to another district pursuant to 28 U.S.C. § 1404(a) as follows:

> For the convenience of parties and witnesses, in the interest of justice, a district court may transfer any civil action to any other district or division where it might have been brought.

A transfer pursuant to 28 U.S.C. § 1404(a) may be made on the court's own motion *Lead Industries Association, Inc.* v. *Occupational Safety and Health Administration,* 610 F.2d 70, 79-80 n.17 (2d Cir. 1979); *see National Acceptance Co.* v. *Wechsler,* 489 F. Supp. 642, 649 (N.D. Ill. 1980); *Riordan* v. *W. J. Bremer, Inc.,* 466 F. Supp. 411, 417 (S.D. Ga. 1979) and can be made without reaching the complex questions of personal jurisdiction raised here.[3]

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[3] The Trustees base the court's in personam jurisdiction over Angelos and Howe on the allegedly tortious conduct committed in New York. Howe contends that, under New York's fiduciary shield doctrine, his transaction of business or alleged tortious conduct in this state do not subject him to jurisdiction under New York's long-arm statute, section 302(a)(1) or (2) of New York Civil Practice Law and Rule. *See Marine Midland Bank, N.A.* v. *Miller,* 664 F.2d 899 (2d Cir. 1981). (Angelos seeks to vacate the default judgments entered aaginst him and has not moved to dismiss for lack of personal jurisdiction). The Trustees base personal jurisdiction over the other third-party defendants on the allegation that Angelos and Howe visited New York "with the express authority of and at the express direction of [Bankcorporation's] Board." Trustees' Third-Party Complaints ¶ 11.

The Trustees have the burden of establishing personal jurisdiction *KVOS, Inc.* v. *Associated Press,* 229 U.S. 269, 278, 57 S. Ct. 197, 200-201 (1936); *Forsythe* v. *Overmyer,* 576 F.2d 779, 781 (9th Cir.), *cert. denied,* 439 U.S. 864, 99 S. Ct. 188 (1978). At this state of the proceeding, the Trustees are required to make out a prima facie case, showing jurisdiction. *Data Disc, Inc.* v. *Systems Technology Associates, Inc.,* 557 F.2d 1280, 1285 (9th Cir. 1977).

(footnote continued on following page)

Memorandum of Decision and Order
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Transfer may be directed pursuant to § 1404(a) by a court without personal jurisdiction over the defendants. *Corke* v. *Sameiet M. S. Song of Norway,* 572 F.2d 77 (2d Cir. 1978); *Volk Corp.* v. *Art. Pak Clip Art Service,* 432 F. Supp. 1179, 1181 (S.D.N.Y. 1977).

(footnote continued from previous page)

The court does not here determine the applicability of New York's fiduciary shield doctrine. *See Marine Midland Bank, N.A.* v. *Miller, supra; Laufer* v. *Ostrow,* 55 N.Y. 305, 313-14, 449 N.Y.S. 2d 456, 460-61 (1982). That doctrine has been criticized when asserted on behalf of a corporate agent who committed a tort while in this state. *See Agra Chemical Distributing Co.* v. *Marion Laboratories, Inc.,* 523 F. Supp. 669 (W.D.N.Y. 1981); *Merkel Associates, Inv.* v. *Bellofram Corp.,* 437 F. Supp. 612, 618-10 (W.D.N.Y. 1981). Nonetheless, the United States Court of Appeals for the Second Circuit applied the fiduciary shield doctrine in *Marine Midland Bank, N.A.* v. *Miller, supra,* where the New York plaintiff bank had extended a loan based upon the allegedly false representations of the out-of-state individual defendant on the grounds that it was "unfair to force an individual to defend a suit brought against him personally in a forum with which his only relevant contacts are acts performed not for his own benefit but for the benefit of his employer." 664 F.2d at 902. The court then found that the corporate employer was a mere shell for the individual's personal activities, concluding that the fiduciary shield doctrine did not apply in such situation. Here, the Trustees have not alleged that Bankcorporation is a shell or that Howe (or Angelos) acted in New York for his own benefit rather than for the benefit of Bankcorporation.

Additionally, the Trustees fail to offer any proof respecting a basis for jurisdiction over the other third-party defendants pursuant to § 302(a)(1)(2) or (3). *See, e.g., Hargrave* v. *Oki Nursery, Inc.,* 636 F.2d 897 (2d Cir. 1980) (court found jurisdiction over foreign corporate defendant under § 302(a)(3) for false representations made without the state). To make out a prima facie case, Trustees are required to "do more than rely on merely conclusory allegations like those pleaded in paragraph [11 of the complaints]." *Shaw* v. *American Cyanamid Co.,* 534 F. Supp. 527, 528 (D. Conn. 1982). The Trustees do not submit proof of other contacts. A letter by Trustees' counsel submitted at the invitation of the court merely states "there is no question that the Third-Party defendants are subject to this Court's personal jurisdiction

(footnote continued on following page)

Memorandum of Decision and Order dated August 18, 1983

Despite the amount of papers filed in the third-party actions, the court is unable to determine whether these actions "might have been brought" in the Northern District of Illinois since it is not clear (for purposes of venue under § 1391(a) in the proposed transferee district), that all third-party defendants resided in Illinois at the time these actions were brought. *See Hoffman* v. *Blaski*, 363 U.S. 335, 80 S. Ct. 1084 (1960). This court considers the Illinois district court to be the proper forum for litigation of these actions under the standards set forth at § 1404(a),[4] but is unable to direct such tranfer unless venue would have been proper there as well as here. *Shelley* v. *The Macabees*, 191 F. Supp. 742 (E.D.N.Y. 1961). Angelos states that he is a resident of Florida although he gave his address as "300 Birch, Winnetka, Illinois, 60098" on the signature page of the guaranty to the loan agreement. The respec-

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(footnote continued from previous page)

as a result of their own or their agent's fraudulent conduct within this District." Nevertheless, the court concludes that it would be imprudent to dismiss the claims against these third-parties at this stage of the proceedings.

Accordingly, the court makes no determination respecting personal jurisdiction at this time, seeking instead to transfer the Trustees' third-party actions to a district court in Illinois where all defendants can be sued. In the event that such transfer is not possible, the court will grant the Trustees leave to conduct discovery for the limited purpose of establishing a basis for personal jurisdiction. All jurisdictional matters (including, i.e., service of process) will then be treated after the Trustees have had the opportunity to complete discovery and restate their claims in accordance with the memorandum of decision.

[4] Transfer to Illinois is appropriate here. All defendants can be sued in Illinois, all Bank and Bankcorporation records are located there, and that forum is more convenient for witnesses respecting the knowledge or participation, or both, of each defendant in the alleged misrepresentations. *A. Olnick & Sons* v. *Dempster Brothers, Inc.*, 365 F.2d 439, 442 (2d Cir. 1966); *Abramson* v. *INA Capital Management Corp.*, 459 F. Supp. 917, 921 (E.D.N.Y. 1978); *Levine* v. *Financial Programs, Inc.*, 318 F. Supp. 952, 955 (S.D.N.Y. 1969).

tive residences of the other third-party defendants is unknown. Personal jurisdiction over the third-party defendants in Illinois is not at issue. Accordingly, the court invites the Trustees and all third-party defendants to address the issue of transfer under § 1404(a), including (1) the facts respecting residence of the third-party defendants and (2) any opposition to such sua sponte transfer, *e.g.*, on the grounds of prejudice. *See, Swindell-Dressler Corp.* v. *Dumbauld,* 308 F.2d 267, 273-74 (3rd Cir. 1962). Affidavits may be filed on the issue of venue within twenty (20) days from date hereof.

D. *Common Law Fraud*

The Trustees' claims are based, *inter alia,* upon allegations of common law fraud. Rule 9(b), Fed.R.Civ.P. provides:

> In all averments of fraud or mistake, the circumstances constituting fraud or mistake shall be stated with particularity. Malice, intent, knowledge and other condition of mind of a person may be averred generally.

We find that except for the allegations respecting Angelos and Howe, the alleged circumstances constituting fraud have not been stated here against third-party defendants with the degree of particularity required under Rule 9(b). The allegations made respecting Angelos and Howe are sufficiently specific to survive Howe's motion to dismiss. Angelos has not so moved.

The Trustees are hereby granted leave to replead, within twenty (20) days hereof, claims alleging fraud with respect to the other third-party defendants.

E. *Angelos' Motion to Vacate Default*

Anthony G. Angelos moves to vacate defaults entered against him as a result of his failure to timely appear and

answer in the first and second third-party actions herein.[5] The record indicates that third-party summonses and complaints were properly served pursuant to Rule 4(d)(1), Fed.R.Civ.P.

Under Rule 55(c), Fed.R.Civ.P., entry of a default may be set aside by the court for "good cause shown." Angelos denies that he (or his wife) were ever served and states that he is willing to appear and answer the third-party complaints. He states further that he believed that "as a non-resident of the Eastern District of New York, [he] had to be handed the process in person." Angelos Affidavit, ¶ 7(a).

We find that Angelos has a good defense to the said action and conclude that his rights should not be determined without an opportunity to be heard. Further, because of his alleged central role in the events here and his major financial interest in Bankcorporation, participation by Angelos in the third-party actions will permit a more complete development of the facts herein and a more equitable determination of the liability of the various parties before us.

We reject the Trustees' suggestion that, as a condition of vacating these defaults, Angelos should be required to post bond to secure the amount of the default judgment pending trial on the merits. Accordingly, the defaults entered by the Trustees in the Katsaros action and the Donovan action with respect to Anthony G. Angelos are hereby vacated.

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[5] Notice of default as to Angelos was filed April 22, 1983 for failure to respond to the Trustees' third-party complaints. On May 5, 1983, notice of default as to Angelos was filed for failure to answer the Fund's third-party complaints. Angelos filed a motion for relief from defaults on June 15, 1983. Following our dismissal this day of the Fund's third-party action, only the defaults filed in the Trustees' third-party actions are relevant here.

Memorandum of Decision and Order
dated August 18, 1983

Conclusion

The third-party complaints filed by the Fund seeking indemnification in the Katsaros action and the Donovan action are, in all respects, dismissed.

The first and second claims respecting violations of the federal securities statutes as raised by the Trustees as third-party plaintiffs in the Katsaros action and the Donovan action are, in all respects, dismissed.

The Trustees may, within twenty (20) days hereof, replead the third claim (fraud) with respect to third-party defendants, excepting Angelos and Howe.

The Trustees and the third-party defendants may, within twenty (20) days hereof, file affidavits on the issue of venue, including objections to the transfer of this action pursuant to 28 U.S.C. § 1404(a).

The Clerk of the Court is directed to vacate the entries of default against Anthony G. Angelos, and, there being no just reason for delay, the Clerk of the Court is further directed to enter partial judgment pursuant to Rule 54(b), Fed.R.Civ.P., (1) against the Fund and in favor of the third-party defendants, dismissing the second third-party complaint brought by the Fund in the Katsaros action and the Donovan action; and (2) against the Trustees and in favor of the third-party defendants, dismissing the first and second claims of the third-party complaints brought by the Trustees in the Katsaros action and the Donovan action.

So Ordered.

.....

U. S. D. J.

Memorandum of Decision and Order dated December 7, 1983

UNITED STATES DISTRICT COURT

EASTERN DISTRICT OF NEW YORK

CV 81-2277

TED KATSAROS, JOHN KUEBLER, ROBERT TROTT, LAWRENCE KUDLA and CHARLES CURD, as participants in the Teamsters Local 282 Pension Trust Fund,

Plaintiffs,

—against—

JOHN CODY, ROBERT SASSO, JOHN DEE, WILLIAM ARGENTA, RALPH GUERCIA, HERBERT SCHNEIDER and LOUIS NAPPI, as Trustees of the Teamsters Local 282 Pension Trust Fund,

Defendants.

CV 82-1920

RAYMOND J. DONOVAN, Secretary of Labor of the United States Department of Labor,

Plaintiffs,

—against—

JOHN CODY, WILLIAM ARGENTO, JOHN DEE, RALPH GUERCIA, LOUIS G. NAPPI, ROBERT SASSO, HERBERT SCHNEIDER and the TEAMSTERS LOCAL 282 PENSION TRUST FUND,

Defendants.

Memorandum of Decision and Order
dated December 7, 1983

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MISHLER, *District Judge*

On July 21, 1983 the court filed a memorandum of decision after a trial on the issues to the court without a jury. The court concluded that the Trustees breached their fiduciary duty to the participants and beneficiaries of the

Memorandum of Decision and Order dated December 7, 1983

Teamsters Local 282 Pension Trust Fund ("Fund") in violation of Section 404(a)(1)(B) of the Employee Retirement Income Security Act of 1974 ("ERISA"), 29 U.S.C. § 1104(a)(1)(B) in approving a loan of 2 million dollars and disbursing Fund assets in or about February and March 1983 to the Des Plaines Bankcorporation ("Bankcorporation"). The court found the defendant Trustees jointly and severally liable for any and all loss resulting from the default by Bankcorporation and directed a hearing on the issue of damages.[1] Plaintiffs also seek removal of the Trustees from their position of trust and the appointment of an independent asset manager. Plaintiffs in the Katsaros action ask that the court appoint Trustees of the Fund representing the Local 282 from their group.

The court heard argument on the appropriate form of relief on September 12, 1983. The Trustees opposed the entry of judgment on the ground that events subsequent to the trial indicate that all or most of the loss will be recovered in law suits pending against Anthony G. Angelos, president of Bankcorporation, and Jonathan D. [sic] Howe, a director and counsel to Bankcorporation. The Trustees also point to the sale of property obtained by the Fund as security for the loan, said to be more than 1.6 million dollars. They further point to a probable distribution through the efforts of the Federal Deposit Insurance Corporaton in liquidating the assets of Bankcorporation.

The court finds no reason to delay the entry of a judgment against the Trustees in the amount of the loss.

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[1] The court granted judgment in the amount of $23,473.57 representing the sum the Fund lost in the form of legal fees and disbursements by entering into a contract in February 1978 with one Hyman Green in which the Fund agreed to loan Green 20 million dollars in violation of Section 404(a)(1) of ERISA, 29 U.S.C. § 1104(a)(1). The court enjoined performance by the Fund. *Marshall* v. *Teamsters Local 282 Pension Trust Fund*, 458 F. Supp. 986 (E.D.N.Y. 1978).

Memorandum of Decision and Order
dated December 7, 1983

Payments received by the Fund on account of the loan will be credited against the judgment sum. The right to injunctive relief or appointment of an asset manager does not depend on the good fortune or misfortune in obtaining reimbursement from third parties, but whether based on past performance, the Fund is exposed to mismanagement in continuing the present Trustees in office or in allowing a system that invites and tolerates mismangement to continue.

Monetary Loss

No material issue is in dispute with relation to the amount of the Fund's loss. The court finds the loss as follows:

Unpaid balance	$1,625,000.00
Interest erroneously computed (See memo of decision note 6)	32,500.00
Interest as provided in the loan agreement from 9/1/80 (date of last payment) to 3/1/83 (date of maturity of loan)	700,453.00
Interest from 3/1/83 to 12/15/83 at governing prime rate of 11% on $1,625,000 (9½ months)	141,512.00
SUB TOTAL	$2,499,465.00
Due Fund on sub total failure to reimburse it for fees paid on Green loan (against all defendant Trustees except Guercia)	23,473.00

Memorandum of Decision and Order dated December 7, 1983

Interest from 8/11/78 (date of decision in *Donovan* v. *Local 282 Pension Trust Fund)* to 12/15/83 at legal rate of 9% (5 years, 4 mos., 4 days)	7,126.00
SUB TOTAL	$ 30,599.00
GRAND TOTAL	$2,530,064.00

The Management of the Fund

The Fund operates under the authority and supervision of six Trustees. Three employer Trustees and three union Trustees are nominated and elected by all employers who, under the terms of their labor contract with Local 282, are parties to the Trust Agreement. The union Trustees are appointed by the Executive Board of Local 282.[2]

Defendant Cody is the Fund's manager. He is the chief administrator of the Fund and receives a salary from the Fund. He is also a trustee of the fund and president of Local 282 and receives a salary of $100,776 per year as president of the local. The employer Trustees, with rare exception, have labor contracts with Local 282.[3] The economic power that Cody wields over both employer and union Trustees gives him complete control of the policies

[2] The Trustees of the Fund also serve as trustees of the Welfare and Annuity Trust Funds. See Declaration of Trust.

[3] The court notes the common practice in the composition of an employee benefit plan to elect (or appoint) employer Trustees who have labor contracts with a union. Often union officials are also Trustees. First there is a built-in conflict of interest in a union official who negotiates a loan contract to also serve as a Trustee of a Fund that receives contributions under the labor contract. Second, the power of the labor leader over the employer trustee deprives the trustee of the free exercise of his opinion.

and practices of the Fund.[4] The manner in which the Bankcorporation loan was approved is evidence of that domination. The reasons for making the loan are unclear. Cody testified that he met Angelos socially a few times and knew him to be a public official in the State of Illinois (Commission of Insurance). For whatever reason, this was a loan that Cody decided to make and make quickly.

Cody has a history of breaches of his fiduciary duty to the Fund. In *U.S.* v. *Cody*, 82 CR 00013(S) Cody was convicted after trial to a jury of: 18 U.S.C. § 1962(c) (Racketeer Influenced and Corrupt Organizations Act), three counts based on 29 U.S.C. § 186(b)(1),[5] income tax evasion in filing a false and fraudulent return for the calendar year 1975 (26 U.S.C. § 7201), and filing a false tax return for the year 1975 (26 U.S.C. § 7206). The income tax violations resulted from Cody's failure to report a kickback of $100,000 he demanded from one John Strong, a real estate broker, in exchange for his help in arranging the purchase by the Fund of a 90 acre parcel of undeveloped land near Riverhead, Long Island.

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[4] In a rare instance in which a union Trustee proposed a reduction in the age for early retirement benefits the employer trustees recorded their opposition. From all this court has learned of Cody's power, it is likely that the employer Trustees would have bowed to his wishes, had Cody mad [sic] it clear and firm.

[5] Cody was convicted of four counts based on 29 U.S.C. § 186 (b)(1). Count Two was reversed, slip op. (2d Cir. Nov. 28, 1983) on the ground that no employer/employee relationship existed between Sigmund Somer Construction Company, who gave Cody's mistress, Marilyn Taggert the rent free use of a luxury apartment and garage spaces at North Shore Towers from 1975 to 1977 (valued at about $1,200 per month), and members of Local 282.

Memorandum of Decision and Order
dated December 7, 1983

Removal of Cody as Fund Manager
and Removal of Trustees

"Where there has been a breach of fiduciary duty, ERISA grants to the courts broad authority to fashion remedies for redressing the interests of participants and beneficiaries." *Donovan* v. *Mazzola, et al.,* 716 F.2d 1226 (9th Cir. 1983) (citing *Eaves* v. *Penn,* 587 F.2d 453, 462 (10th Cir. 1978); *Marshall* v. *Snyder,* 572 F.2d 894, 901 (2d Cir. 1978)). Courts have a duty to fashion a remedy that would protect the Fund's assets from dissipation through breaches of the fiduciary duty and responsibility imposed on Trustees and ERISA, *Donovan* v. *Mazzola, et al., supra* at 1235; *Eaves* v. *Penn, supra* at 462; *Marshall* v. *Glass/Metal,* 507 F. Supp. 378, 385 (D. Ha. 1980); *Freund* v. *Marshall & Ilsley Bank,* 485 F. Supp. 629, 643 (W.D. Wis. 1979). This includes the power and the duty to appoint an investment manager with full and complete authority to invest and reinvest the Fund's assets and appoint an administrator of the Fund to oversee the day-to-day activities of the Fund, including determinations of applications for benefits, payment of benefits, receipt of contributions from employers, etc.[6]

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[6] The House and Senate reports which the Congress considered in enacting ERISA expressed the intent of Congress to invest the power and impose the duty on the federal courts to safeguard the financial integrity of employee benefit funds. The House Committee report No. 93-533 states:

> The intent of the Committee is to provide the full range of legal and equitable remedies available in both state and federal courts and to remove jurisdictional and procedural obstacles which in the past appear to have hampered effective enforcement of fiduciary responsibilities under state law or recovery of benefits due to participants.

3 U.S. Code Cong. & Admin. News 93rd Cong., 2d Session at p. 4871.

(footnote continued on following page)

Memorandum of Decision and Order dated December 7, 1983

The court hereby directs that Cody be removed from his position as fund manager, and Cody, Sasso, Dee, Argenta [sic], Schneider and Nappi are hereby removed and they shall not hereafter exercise the authority vested in them except to transfer control of the management of the Fund and its assets to the court appointed asset manager and fund manager.

The court nominates, constitutes and appoints Albert B. Lewis, 40 Wall Street, New York, New York until March 31, 1985 as assets manager with full and complete control over the assets of the Fund with authority to invest and reinvest the Fund's assets. The asset manager may, subject to the approval of the court, employ the services of investment experts and consultants that he deems reasonably necessary to attain the most favorable return consistent with Section 404(a)(1) of ERISA, 29 U.S.C. § 1104(a)(1).

The asset manager shall maintain records of the Fund including bank accounts relating to the Fund's assets.

(footnote continued from previous page)

The Senate Committee report No. 93-383 states:

> Appropriate equitable relief may be granted in a civil action. For example, injunctions may be granted to prevent a violation of fiduciary duty, and a constructive trust may be imposed on the plan assets, if needed to protect the participants and beneficiaries. Also, the bill specifically provides that a fiduciary may be removed through civil action brought by the Secretary or participants or beneficiaries if he has violated any of the specified obligations, or is serving in violation of the criminal conviction provisions (the Attorney General also may bring an action to remove in the latter case). It is expected that a fiduciary (other than one serving in violation of the criminal conviction provisions) may be removed for repeated or substantial violations of his responsibilities, and that upon removal the court may in its discretion, appoint someone to serve until a fiduciary is properly chosen in accordance with the plan.

3 U.S. Code & Admin. News 93rd Cong., 2d Session, p. 4989.

The asset manager is directed to file quarterly reports beginning March 31, 1984. Said reports shall be filed within thirty (30) days after the end of each period.

The court nominates, constitutes and appoints Joseph Jaspan, 200 Garden City Plaza, Garden City, New York as fund manager until March 31, 1985 with full power and authority over the management of the day-to-day activities of the Fund, including but not limited to:

(a) Determining applicants' rights to benefits under the plan.

(b) Payment of benefits to beneficiaries.

(c) Collection of contributions to the Plan.

(d) Employing and discharging employees of the Plan.

The fund manager shall have the authority to employ a management consultant to report on the condition of the Fund and make recommendations.

Cody, as fund manager and trustee, and the trustees of the Fund shall immediately turn over all the books and records of the Fund and execute any and all documents necessary to give the asset manager and fund manager control of the matter respectively delegated to them.

On February 1, 1985, at 9:00 a.m., the court will invite interested parties to present their views on the advisability of continuing the asset manager and/or the fund manager beyond the date fixed for termination of their respective positions.

The Welfare and Annuity Funds

What has been said of Cody's conduct and that of the trustees in the performance of their duties to the Pension Fund applies to the Welfare and Annuity Funds. The court directs the plaintiffs to take appropriate action

with a view to removing them from their fiduciary positions in those funds. *See Marshall* v. *Snyder, supra* at 902.

Attorney's Fees Requested by Hall, Clifton & Schwartz, Attorneys for Plaintiff Participants in Fund

This action was vigorously defended and the claims stubbornly resisted by defendants. The plaintiff participants alone carried the burden of pressing the action that ultimately resulted in a significant financial benefit to both participants and beneficiaries. When the Secretary commenced his action, the burden was lightened. The defense to the claims were meritless. The tactics employed were in some instances for the purpose of delay and employed in bad faith, e.g., multiple third-party actions, motions for stay of entry of judgment. An award of attorney's fees and costs would deter others charged with ERISA violations to interpose frivolous, meritless defenses.

The court will award reasonable attorney's fees and expenses. Section 502(g), 29 U.S.C. § 1132(g), *Iron Workers Local No. 272* v. *Bowen,* 624 F.2d 1255, 1266 (5th Cir. 1980); *Birmingham & Morano* v. *So Gen-Swiss Intern. Corp.,* 529 F. Supp. 86, 92 (S.D.N.Y. 1981), *aff'd,* —— F.2d —— (2d Cir. 1983).

Consolidation of Actions

The above actions were consolidated for trial. The court finds it convenient to consolidate the actions for all purposes. The Clerk shall enter a judgment to be approved by the court as the judgment of this consolidated action.

So Ordered.

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U. S. D. J.

Judgment

UNITED STATES DISTRICT COURT
EASTERN DISTRICT OF NEW YORK

CV 81-2277

TED KATSAROS, JOHN KUEBLER, ROBERT TROTT, LAWRENCE KUDLA and CHARLES CURD, as participants in the Teamsters Local 282 Pension Trust Fund,

Plaintiffs,

—against—

JOHN CODY, ROBERT SASSO, JOHN DEE, WILLIAM ARGENTA, RALPH GUERCIA, HERBERT SCHNEIDER and LOUIS NAPPI, as Trustees of the Teamsters Local 282 Pension Trust Fund,

Defendants.

CV 82-1920

RAYMOND J. DONOVAN, Secretary of Labor of the United States Department of Labor,

Plaintiffs,

—against—

JOHN CODY, WILLIAM ARGENTO, JOHN DEE, RALPH GUERCIA, LOUIS G. NAPPI, ROBERT SASSO, HERBERT SCHNEIDER and the TEAMSTERS LOCAL 282 PENSION TRUST FUND,

Defendants.

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This consolidated action having come on for trial before the court, Hon. Jacob Mishler, District Judge, presiding and the issues having been duly tried and a decision on the issue of liability dated July 21, 1983 having been duly rendered, and a decision on the issue of damages and the appropriate relief dated December 7, 1983 having been duly rendered, now therefore, it is

ORDERED, ADJUDGED AND DECREED

1. that the Teamsters Local 282 Pension Fund recover of defendants John Cody, William Argento, John Dee, Ralph Guercia, Louis G. Nappi, Robert Sasso and Herbert Schneider, jointly and severally the sum of

$2,530,064.00 (except that defendant Ralph Guercia's liability is reduced by $30,599) together with interest from December 15, 1983, together with costs and disbursements and legal fees and expenses payable to plaintiffs Ted Katsaros, etc. for legal services rendered by Hall, Clifton & Schwartz, and it is further

ORDERED, ADJUDGED AND DECREED

2. that the defendants are hereby restrained, enjoined and prohibited from exercising any authority granted under the trust agreement or Plan or any other document as trustees of the Fund, and defendant John Cody is similarly restrained, enjoined and prohibited from exercising any authority as fund administrator; and it is further

ORDERED, ADJUDGED AND DECREED

3. that Albert B. Lewis, Esq., 40 Wall Street, New York New York, be and he hereby is appointed asset manager with full and complete authority to invest, and reinvest the assets of the Teamsters Local 282 Pension Trust Fund and to open and maintain bank accounts in the name of the Teamsters Local 282 Pension Trust Fund. All checks, drafts or orders for payment shall be countersigned by the Clerk of the Court, and it is further

ORDERED, ADJUDGED AND DECREED

4. that Joseph Jaspan, Esq., 200 Garden City Plaza, Garden City, New York, be and he hereby is appointed fund manager of the Teamsters Local 282 Pension Trust Fund with full and complete authority over the day-to-day management of the affairs of the Fund. The said fund manager is authorized to open and maintain bank accounts in the name of the Teamsters Local 282 Pension Trust Fund. All checks, drafts or orders for payment

shall be made by the fund manager and the administrator of the Fund; the fund manager may designate an employee other than the administrator of the Fund as an authorized individual to counter-sign checks, drafts or orders of payment signed by him. He may issue checks, or drafts for benefit payments and payroll by imprinting the authorized signature through computer or other electronic or mechanical device, and it is further

ORDERED, ADJUDGED AND DECREED

5. that the asset manager and the fund manager shall serve without bond.

Dated: Uniondale, N.Y.
December 7, 1983

.....
Clerk

Approved as to form

.....
U. S. D. J.

Memorandum of Decision and Order

UNITED STATES DISTRICT COURT

EASTERN DISTRICT OF NEW YORK

CV 81-2277

TED KATSAROS, JOHN KUEBLER, ROBERT TROTT, LAWRENCE KUDLA and CHARLES CURD, as participants in the Teamsters Local 282 Pension Trust Fund,

Plaintiffs,

—against—

JOHN CODY, ROBERT SASSO, JOHN DEE, WILLIAM ARGENTO, RALPH GUERCIA, HERBERT SCHNEIDER and LOUIS NAPPI, as Trustees of the Teamsters Local 282 Pension Trust Fund,

Defendants.

CV 82-1920

RAYMOND J. DONOVAN, Secretary of Labor of the United States Department of Labor,

Plaintiffs,

—against—

JOHN CODY, WILLIAM ARGENTO, JOHN DEE, RALPH GUERCIA, LOUIS G. NAPPI, ROBERT SASSO, HERBERT SCHNEIDER and the TEAMSTERS LOCAL 282 PENSION TRUST FUND, WELFARE TRUST FUND, ANNUITY TRUST FUND, and LEGAL SERVICES TRUST FUND,

Defendants.

Memorandum of Decision and Order

APPEARANCES:

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Edward J. Boyle, Esq., *Of Counsel*

O'CONNOR & MANGAN, P.C.
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Local 282 Pension Trust Fund
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Queens Plaza
Long Island City, New York 11101
J. Warren Mangan, Esq., *Of Counsel*

MISHLER, *District Judge*

The law firm of Hall, Clifton & Schwartz applies for counsel fees and disbursements pursuant to 29 U.S.C. § 1132(g) for services rendered in *Katsaros, et al.* v. *Cody, et al.*, and the Secretary seeks reimbursement for

fees paid to court reporters for transcripts and the taking of depositions pursuant to 28 U.S.C. § 1920 and Rule 54(d) of the Fed.R.Civ.P.

Claim of Hall, Clifton & Schwartz

The affidavit of Arthur G. Schwartz asserts a claim of $95,275 for attorney's fees and $901.46 for disbursements —a total of $96,176.46. The demand is based on the following calculations:

	Hours	*Rate Per. Hr.*	
Schwartz	234.05[1]	$150	$36,457.50
Jennik	111.8	100	11,180.00
			$47,637.50
		A Multiplier	2
			$95,275.00
		Disbursements	901.46
		TOTAL	$96,176.46

Of the 234.05 hours claimed by Schwartz, 37.5 hours were spent attending depositions, 23 hours were spent attending court for hearings on motions and for the trial, and 173.55 hours were spent reviewing reports, motion papers [sic] letters, etc. and making telephone calls.

Of the 111.8 hours claimed by Susan M. Jennik, 9 hours were spent attending depositions and 18 hours attending court for hearings on motions and trial. The balance of 84.8 hours is almost entirely for research and drafting memoranda of law and motions.

[1] This figure includes 10.75 hours preparing the motion for the award of fees but does not include the time for the hearing on the motion.

Schwartz was admitted to practice law in the State of New York in January 1979.[2] At that time he opened a private law practice specializing in labor law. He joined Hall, Clifton & Schwartz in February 1980. Since January 1979, Schwartz has acted as general counsel to several labor unions and employee associations. He has represented unions and employees at hearings before hearing examiners of the National Labor Relations Board and has appeared in federal district courts pressing claims of unions and employees relating to labor relations.

Susan M. Jennik was admitted to practice law in June 1982. She has appeared before the National Labor Relations Board, The Merit Systems Protection Board of the New York State Division of Human Rights and the City Commission on Human Rights.

The court conducted a hearing on the application. The testimony of Schwartz & Jennik generally restated the affidavits submitted in support of the motion. The only significant fact that the hearing revealed was that Schwartz charges his union clients at the rate of $75 per hour. Defendants offered no evidence in opposition but rested on the affidavit in opposition.

Discussion

The Court in *Hensley* v. *Eckerhart*, —— U.S. ——, 103 S. Ct. 1933, 1937, n.3 (1983) listed twelve factors to be considered in determining a reasonable attorney's fee to be awarded a prevailing party under the Civil Rights Attorneys Fees Award Act of 1976, 42 U.S.C. § 1988:

1. the time and labor required;

2. the novelty and difficulty of the questions;

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[2] From March 1978 to November 1978 he was employed as a staff attorney at Bronx Legal Services.

3. the skill requisite to perform the legal service properly;

4. the preclusion of employment by the attorney due to acceptance of the case;

5. the customary fee;

6. whether the fee is fixed or contingent;

7. time limitations imposed by the client or the circumstances;

8. the amount involved and the results obtained;

9. the experience, reputation and ability of the attorneys;

10. the "undesirability" of the case;

11. the nature and length of the professional relationship with the client; and

12. awards in similar case.

All the factors are not applicable to the subject matter in this action, i.e., (4) (10) and (11). The factors present in this case are the services rendered on behalf of the Secretary and the reliance by Schwartz on the skill, experience and effort of the government lawyers.

The Court in *Hensley* observed: "The most useful starting point for determining the amount of a reasonable fee is the number of hours reasonably expended on the litigation multiplied by a reasonable hourly rate." *Id.* U.S. at ——, S. Ct. at 1939. [sic] *See Copeland* v. *Marshall,* 641 F.2d 880, 891 (D.C. Cir. 1980); *Cohen* v. *West Haven Bd. of Police Com'rs,* 638 F.2d 496, 505 (2d Cir. 1980); *City of Detroit* v. *Grinnell Corp.,* 560 F.2d 1093, 1098 (2d Cir. 1977).

In determining [sic] reasonable hourly rate for legal services, the court has the obligation of assigning the appropriate rate for the different levels of expertise as in-

dicated by the attorney's position in the firm. The rate fixed should also reflect the different kinds of services performed by the same attorneys. *Miles* v. *Sampson,* 675 F.2d 5, 9 (1st Cir. 1982); *Copeland* v. *Marshall, supra* at 892.

I find the number of hours for the services rendered to be as claimed.[3] I find the hourly rate for the two classes of services performed by Schwartz and Jennik as follows:

Schwartz	
Attendance at depositions and court 60.5 hours @ $125 per hour	$7,562.50
Other services 173.55 hours @ $75 per hour	$13,016.25
Jennik	
Attendance at depositions and court 27 hours @ $60 per hour	$1,620.00
Other services 84.8 hours @ $50 per hour	$4,240.00
Total	$26,438.75

A discrepancy exists between Jennik's time record and her affidavit. I charge five (5) hours of her time at $50 per hour against the sum found due. I credit the applicants with 7.5 hours at $125 per hour for in court services (by Mr. Clifton) on January 9, 1984 in prosecuting the fee application.[4] The net credit to the applicant is $687.50.

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[3] Though the claim relating to punitive damages was dismissed, the time spent in opposing the motion to dismiss the claim is insignificant.

[4] I deny Schwartz and Jennik reimbursement for their attendance on January 9, 1984. They appeared as witnesses. I further

(footnote continued on following page)

The court finds that the fair and reasonable value of the services rendered by Hall, Clifton and Schwartz is $27,126.25. This "lodestar" figure may be adjusted upward or downward where the case presents novel and complex issues, or the quality of the representation demonstrates exceptional skill. *New York Association for Retarded Children* v. *Carey Inc.*, 711 F.2d 1136, 1144 (2d Cir. 1983); *Cohen* v. *West Haven Bd. of Police Com'rs, supra* at 505.

The so called "multiplier" or "bonus" should not be routinely applied. Though the case was not the "run of the mill" litigation, it was not the kind of case that presented novel and complex legal and factual issues. Hall, Clifton & Schwartz relied to some extent on the support of the government. The court will not increase the fee as found for the reasons urged by applicants.

The court awards applicants' disbursements of $901.46 incurred prior to the fee application and the sum of $100.83 incurred in the fee application or a total of $1,002.29.

The Clerk is directed to add to the amended judgment dated December 27, 1983 the following:

> Plaintiffs are awarded the sum of $28,128.54 as and for legal fees and disbursements in accordance with the memorandum of decision and order dated January 20, 1984, payable to Hall, Clifton and Schwartz.

(footnote continued from previous page)

deny applicants reimbursement for services on January 10, 1984. Applicants failed to produce the records at the hearing the previous day. Defendants' counsel returned to court on January 10, 1984 to inquire as to these inconsistencies. Applicants should not be rewarded for their errors—insignificant as it turned out to be. *New York Association for Retarded Children* v. *Carey*, 711 F.2d 1136, 1148 (2d Cir. 1983).

Memorandum of Decision and Order

Claim of the Secretary

Defendants' opposition to the Secretary's application for costs is based on Section 501(g)(1) of ERISA, 29 U.S.C. § 1132(g)(1). That section provides:

> In any action under this title (other than an action described in paragraph 2) by a participant, beneficiary, or fiduciary, the court in its discretion may allow reasonable attorney's fee and costs of the action to either party.

Defendants argue from there that the omission of the Secretary from that favored group indicates a Congressional intent to deny the Secretary costs that are otherwise taxable under 28 U.S.C. § 1920 and Rule 54(d) of the Fed.R.Civ.P. We disagree. We believe a fair interpretation of the section is only to deny the Secretary "a reasonable attorney's fee" while granting the right to "a participant, beneficiary or fiduciary."

Rule 54(d) provides for taxation of costs to the prevailing party "[e]xcept when express provision therefore is made in a statute of the United States or in these rules." § 1132(g)(1) does not expressly deny the Secretary taxable costs. A prevailing party is presumed to be entitled to taxable costs. *True Temper Corp.* v. *C.F. & I. Steel Corp.*, 601 F.2d 495 (10th Cir. 1979).

The Clerk is directed to tax costs in favor of the Secretary as follows:

Fees of court reporter for transcripts necessarily obtained for use in the case	$2,073.41
Costs incident to the taking of depositions	7,342.69
Total	$9,416.10

So Ordered.

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U. S. D. J.

Amended Judgment

UNITED STATES DISTRICT COURT

EASTERN DISTRICT OF NEW YORK

CV 81-2277

TED KATSAROS, JOHN KUEBLER, ROBERT TROTT, LAWRENCE KUDLA and CHARLES CURD, as participants in the Teamsters Local 282 Pension Trust Fund,

Plaintiffs,

—against—

JOHN CODY, ROBERT SASSO, JOHN DEE, WILLIAM ARGENTA, RALPH GUERCIA, HERBERT SCHNEIDER and LOUIS NAPPI, as Trustees of the Teamsters Local 282 Pension Trust Fund,

Defendants.

CV 82-1920

RAYMOND J. DONOVAN, Secretary of Labor of the United States Department of Labor,

Plaintiffs,

—against—

JOHN CODY, WILLIAM ARGENTO, JOHN DEE, RALPH GUERCIA, LOUIS G. NAPPI, ROBERT SASSO, HERBERT SCHNEIDER and the TEAMSTERS LOCAL 282 PENSION TRUST FUND, WELFARE TRUST FUND, ANNUITY TRUST FUND, and LEGAL SERVICES TRUST FUND,

Defendants.

Amended Judgment

APPEARANCES:

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Attorneys for Defendant Teamsters
Local 282 Pension Trust Fund
The Chase Manhattan Building
Queens Plaza
Long Island City, New York 11101
J. Warren Mangan, Esq., *Of Counsel*

This consolidated action having come on for trial before the court, Hon. Jacob Mishler, District Judge, presiding and the issues having been duly tried and a decision on the issue of liability dated July 21, 1983 having been duly rendered, and the court having held a hearing

on December 20, 1983 on plaintiffs' motion and made its decision in open court, now therefore, it is

ORDERED, ADJUDGED AND DECREED

1. that the Teamsters Local 282 Pension Fund recover of defendants John Cody, William Argento, John Dee, Ralph Guercia, Louis G. Nappi, Robert Sasso and Herbert Schneider, jointly and severally the sum of $2,530,064.00 (except that defendant Ralph Guercia's liability is reduced by $30,599) together with interest from December 15, 1983, together with costs and disbursements and legal fees and expenses payable to plaintiffs Ted Katsaros, etc. for legal services rendered by Hall, Clifton & Schwartz, and it is further

ORDERED, ADJUDGED AND DECREED

2. that the defendants are hereby restrained, enjoined and prohibited from exercising any authority granted under the respective trust agreements or Plans or any other documents as trustees of the Teamsters Local 282 Pension Trust Fund, Welfare Trust Fund, Annuity Trust Fund, and Legal Services Trust Fund, and defendant John Cody is similarly permanently restrained, enjoined and prohibited from exercising any authority as Fund administrator; and it is further

ORDERED, ADJUDGED AND DECREED

3. that Albert B. Lewis, Esq., 40 Wall Street, New York, New York, be and he hereby is appointed asset manager to and including March 31, 1985, with full and complete authority to invest, and reinvest the assets of the Teamsters Local 282 Pension Trust Fund, Welfare Trust Fund, Annuity Trust Fund, and Legal Services Trust Fund, and to open and maintain bank accounts in the names of

the respective Funds. All checks, drafts or orders for payment shall be countersigned by the Clerk of the Court, and it is further

ORDERED, ADJUDGED AND DECREED

4. that Joseph Jaspan, Esq., 200 Garden City Plaza, Garden City, New York, be and he hereby is appointed Fund manager to and including March 31, 1985, of the Teamsters Local 282 Pension Trust Fund, and commencing 12:01 a.m., January 3, 1984, is appointed as Fund manager of the Welfare Trust Fund, Annuity Trust Fund, and Legal Services Trust Fund, with full and complete authority over the day-to-day management of the affairs of the respective Funds. The Fund manager is authorized to employ a Fund administrator (or assistant Fund manager). The said Fund manager is authorized to open and maintain bank accounts in the names of the respective Funds. All checks, drafts or orders for payment shall be made by the Fund manager and the administrator of the Funds; the Fund manager may designate an employee other than the administrator of the Funds as an authorized individual to counter-sign checks, drafts or orders of payment signed by him. He may issue checks, or drafts for benefit payments and payroll by imprinting the authorized signatures through computer or other electronic or mechanical device, and it is further

ORDERED, ADJUDGED AND DECREED

5. that the asset manager and the Fund manager shall serve without bond, and it is further

ORDERED, ADJUDGED AND DECREED

6. that any persons appointed as successor trustees of the Teamsters Local 282 Pension Trust Fund, Welfare Trust Fund, Annuity Trust Fund, and Legal Services

Trust Fund shall have no authority with respect to the investments, administrative functions and operations, or any other matters relating to the respective Funds during the term or terms of the investment manager and Fund manager as herein provided or any extended term; and it is further

ORDERED, ADJUDGED AND DECREED

7. that execution of the monetary judgment directed in paragraph 1 shall be stayed upon defendants filing a supersedas bond pursuant to Fed.R.Civ.P. 73(d) in the amount of $1.7 million.

Dated: Uniondale, N.Y.
December 27, 1983

.....
Deputy Clerk

Approved as to form

.....
U. S. D. J.

Memorandum Opinion and Order

IN THE

UNITED STATES DISTRICT COURT

FOR THE NORTHERN DISTRICT OF ILLINOIS
EASTERN DIVISION

No. 84 C 1312

TEAMSTERS LOCAL 282 PENSION TRUST FUND,
Plaintiff,

v.

ANTHONY G. ANGELOS, et al.,
Defendants.

Teamsters Local 282 Pension Trust Fund ("Fund") sues ten defendants,[1] charging them with:

1. violation of Securities Act of 1933 §17(a), 15 U.S.C. §77q(a) ("Section 17(a)") (Count I);

2. violation of Securities Exchange Act of 1934 §10(b), 15 U.S.C. §78j(b) ("Section 10(b)") and related SEC Rule 10b-5 (Count II);

3. common law fraud (Count III); and

4. negligent misrepresentation (Count IV).

Several of the defendants now move for summary judgment under Fed. R. Civ. P. ("Rule") 56, contending the

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[1] Defendants originally comprised nine directors of Des Plaines Bancorporation, Inc. ("Bancorporation")—Anthony G. Angelos, C.J. Bassler, Jr., Jonathan T. Howe, Clarence L. Jensen, Lambrose Karkazis, James C. Kirie, James Kokonas, James Verros and Herbert C. Wenske (collectively "Directors")—and the law firm of Jenner & Block. Fund has since elected to dismiss its claims against directors Verros and Wenske.

present action is barred by collateral estoppel.[2] For the reasons stated in this memorandum opinion and order, that motion is granted and the action is dismissed as to all defendants.

Facts[3]

In 1981 certain Fund beneficiaries sued Fund's Trustees ("Trustees") under 29 U.S.C. §1104(a) for breach of their fiduciary duty, challenging Trustees' actions in connection with a loan to Bancorporation and its wholly-owned subsidiary, Des Plaines Bank ("Bank"). In 1982 the Secretary of Labor commenced an action against Trustees alleging the same breach of duty.[4] In both actions Fund was joined as a defendant, and after the actions were consolidated for pretrial purposes both Fund and Trustees brought third-party actions in each case against Directors and their law firm, alleging the same claims set forth in this action.[5]

In July 1983 District Judge Jacob Mishler issued his findings and conclusions based upon the evidence adduced during his bench trial, *Katsaros* v. *Cody,* 568 F.Supp. 360 (E.D. N.Y. 1983). Several findings were plainly relevant for current purposes (*id.* at 367):

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[2] Defendants have also argued (a) Counts I and II are barred by the statute of limitations and (b) Count IV's theory is legally unavailable to Fund. Because this Court finds the collateral estoppel argument persuasive, these other arguments need not be addressed.

[3] This recitation of facts is drawn from the parties' submissions. Of course any inferences reasonably to be drawn from the established facts are viewed in the light most favorable to the nonmovant Fund. *Korf* v. *Ball State University,* 726 F.2d 1222, 1226 (7th Cir. 1984).

[4] Both actions were filed in the United States District Court for the Eastern District of New York.

[5] Those third party actions were severed from the main cases and eventually dismissed as not procedurally appropriate.

1. Trustees violated their fiduciary duty by failing to make an independent investigation of Bancorporation's and Bank's financial situation.

2. Such duty to make an independent investigation included the duty not to rely on Directors' "representations, predictions and hopes."

3. If Trustees had made an independent investigation, they would have discovered it was imprudent to make the loan to Bancorporation and Bank based upon the financial information presented by Directors.

If those determinations adverse to Trustees are similarly binding as to Fund here, this action must fail for obvious reasons. All Fund's claims rest on asserted misrepresentations on which Fund claims to have relied. If Fund had no right to rely on those representations (indeed had the duty *not* to do so), an essential linchpin to all its claims is missing. Hence this opinion turns to a consideration of whether collateral estoppel applies against Fund, as it clearly would against Trustees.

Collateral Estoppel

Three determinations must be made to apply collateral estoppel as to an issue in a later proceeding:

1. Is the relevant issue in the second suit the same as an issue in the first?

2. Was that issue actually and necessarily litigated and determined in the first suit?

3. Did the party against whom estoppel is asserted have a "full and fair opportunity" to litigate the issue?

Kremer v. *Chemical Construction Corp.*, 456 U.S. 461, 480-81 (1982); *Whitley* v. *Seibel*, 676 F.2d 245, 248, 250 (7th Cir.), *cert. denied*, 103 S.Ct. 254 (1982).

Memorandum Opinion and Order

1. *Two Actions With the Same Issue*

Each of the four theories asserted by Fund here shares an essential element in common with the others—Fund must have relied on Directors' representations *justifiably*:

> 1. As to Count I (on the perhaps questionable assumption Fund has *any* cause of action under Section 17(a), as to which see *Caliber Partners, Ltd.* v. *Affeld*, No. 83 C 6968 slip op. at 8-9 nn. 9-12 (N.D. Ill. Apr. 4, 1984)): *Peoria Union Stock Yards Co.* v. *Penn Mutual Life Ins. Co.*, 698 F.2d 320, 323 (7th Cir. 1983) ("Rule 10b-5 tracks section 17(a) closely"); *Walck* v. *American Stock Exchange, Inc.*, 687 F.2d 778, 789 n.16 (3d Cir. 1982), *cert. denied*, 103 S.Ct. 2118 (1983); *Kramas* v. *Security Gas & Oil, Inc.*, 672 F.2d 766, 769-70 (9th Cir.), *cert. denied*, 103 S.Ct. 444 (1982) and cases cited therein.
>
> 2. As to Count II: *Zobrist* v. *Coal-X, Inc.*, 708 F.2d 1511, 1516 (10th Cir. 1983); *Atchley* v. *Qonaar Corp.*, 704 F.2d 355, 359 (7th Cir. 1983).
>
> 3. As to Count III: *Central States Joint Board* v. *Continental Assurance Co.*, 117 Ill.App.3d 600, 607, 453 N.E.2d 932, 937 (1st Dist. 1983).
>
> 4. As to Count IV: *Penrod* v. *Merrill Lynch, Pierce, Fenner & Smith, Inc.*, 68 Ill.App.3d 75, 81, 385 N.E.2d 376, 381 (3d Dist. 1979).

In the earlier cases Judge Mishler specifically held Trustees, acting on Fund's behalf, had and *breached* a duty to investigate the very wrongdoing of which Fund now complains. That duty "includes the negative obligation of not relying on the representations . . . of a borrower" (568 F. Supp. at 367). By definition then any such reliance could not have been justifiable. And because the collective ob-

ligation of Trustees was the obligation of Fund,[6] just as the representations of Directors were the representations of Bancorporation and Bank as borrowers, the justifiable-reliance issue as litigated in the New York actions is indeed the same issue that would need to be litigated in this action.[7]

2. *"Actually and Necessarily Litigated and Determined"*

It is beyond cavil that the issue of Trustees' duty to investigate was the foundation of Judge Mishler's holding Trustees guilty of a breach of their fiduciary duty. Even Fund does not really contend otherwise.

3. *Full and Fair Opportunity To Litigate*

At a May 9, 1984 status hearing this Court requested the parties to address what Fund (not Trustees) actually did in the New York lawsuit to litigate the issue. That inquiry was prompted by this Court's concerns:

> 1. whether (as often occurs, for example, with a corporation named in a stockholder derivative action that charges an entire board of directors with wrong-

---

[6] As an artificial "person," Fund must perforce have acted (or failed to act) through its Trustees or other agents. *All* its Trustees were defendants in the New York actions, so in the real world sense (and the legal sense) any claimed distinction between Judge Mishler's decision that *Trustees* were obligated not to rely on Directors' representations and a decision that *Fund* was obligated not to rely on those representations would be totally artificial.

[7] Fund seeks to make much of Judge Mishler's comments about the difference in issues. Those comments are really taken out of context, for Judge Mishler was never called on to consider the relationship of the issues in anything resembling a collateral estoppel context. Be that as it may, it is always the job of the second court, not the first court, to determine the collateral estoppel effect on the first court's decision. See *Car Carriers, Inc.* v. *Ford Motor Co.*, No. 83 C 7517, slip op. at 3-4 (N.D. Ill. Mar. 28, 1984).

doing) Fund may have been merely a passive onlooker in the earlier proceeding; or even

2. whether Fund's interest as the prospective beneficiary of any recovery against Trustees may have led it to try to establish the *non*existence of Trustees' right to rely on Directors' representations, rather than the opposite, in the New York litigation.

In response to this Court's question, Fund argues that even though it was named a defendant in the New York lawsuits, it was a nominal defendant only, joined for procedural purposes. In that capacity, Fund urges, collateral estoppel should not be applied against it. 1B *Moore's Federal Practice* ¶0.411[5], at 439-40 n.5.[8]

But even if Fund may have had a right to be treated as a nominal party in the New York lawsuits, that does not prevent the operation of collateral estoppel if Fund *in fact* actually litigated the critical issue. See *United States* v. *Jensen,* 608 F.2d 1349, 1355 (10th Cir. 1979). Defendants present conclusive evidence that Fund, though represented by its own separate counsel, not Trustee's counsel, vigorously argued before Judge Mishler *against* a finding that Trustees had breached their fiduciary duty. Some of Fund's activities at trial include:

1. making of an opening statement;

2. cross-examination of witnesses;

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[8] Defendants try to avoid any need to examine Fund's own conduct in the New York litigation by arguing Fund is in privity with Trustees, so that Trustees' actions automatically bind Fund. That position is analytically unsound. Fund's common interest, in this situation where Trustees breached their fiduciary duty to Fund and the beneficiaries, lies with the beneficiaries and not Trustees. See *In re Gottheimer,* 703 F.2d 1136, 1139 (9th Cir. 1983). But in any event Fund was itself a *party,* so privity need not be found to estop Fund collaterally so long as it was itself active in the proceedings.

3. filing of a motion for directed verdict;

4. offering and introduction of evidence;

5. making of evidentiary objections; and

6. filing of a post-trial memorandum.

In all those activities Fund was not at all passive or neutral, but actively entered the lists by (and on) the side of Trustees.[9] Fund clearly had and exercised a full and fair opportunity to litigate the issue critical to this proceeding.

In sum, Fund deliberately sided with Trustees in the first round of litigation, maintaining Trustees were innocent of any wrongdoing because they relied on the borrowers' representations. That argument was unsuccessful because Judge Mishler held Trustees had no right to rely—indeed had a duty *not* to rely. Trustees were held culpable Fund cannot now argue afresh Trustees' asserted justifiable

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[9] It was particularly distressing to receive Fund's supplemental memorandum, filed in response to this Court's pointed inquiry at the May 9 status hearing. That memorandum was filed by Fund's lawyers in this case, the *same law firm* and *same lawyer* that had represented *Trustees* before Judge Mishler and have just argued on Trustees' behalf the appeal from Judge Mishler's decision (indeed the lawyer filed an extensive affidavit in this case as to the facts regarding the New York proceedings; perhaps "facts" is a misnomer, for the affidavit followed the frequent New York practice of annexing a jurat to an amalgam of facts, hearsay attribution of information clearly not within the affiant's knowledge, conclusions and legal arguments—it is really a brief rather than a true affidavit). Yet the memorandum says "Fund was merely a formal party" (Mem. 2) and "maintained an entirely passive posture with respect to the imprudence claims asserted against the Trustees" (Mem. 3), though counsel had to know better. Howe's Reply Memorandum put the lie to the proposition with a recital of the active involvement of Fund's counsel in New York (R. Mem. 5-6, citing chapter and verse, including transcript references) and the enclosure of Fund's 34-page post-trial memorandum, which urged dismissal of both New York actions because of plaintiff's claimed failure to prove Trustees' violation of their fiduciary duties under ERISA.

reliance, a necessary prerequisite to recovery on each of Fund's current four theories against Directors.

Conclusion

There is no genuine issue of material fact, and moving defendants are entitled to a judgment as a matter of law. Their motion for summary judgment is granted. Because the collateral estoppel ground supporting their motion forecloses Fund's claims against all defendants, this action is dismissed in its entirety.

Milton I. Shadur
United States District Judge

Date: June 8, 1984

Memorandum of Decision and Order dated August 10, 1984

UNITED STATES DISTRICT COURT

EASTERN DISTRICT OF NEW YORK

CV 81-2277

TED KATSAROS, et al.,

Plaintiffs,

—against—

JOHN CODY, et al.,

Defendants.

JOHN CODY, et al.,

Third-Party Plaintiffs,

—against—

ANTHONY G. ANGELOS, et al.,

Third-Party Defendants.

TEAMSTERS LOCAL 282 PENSION TRUST FUND,

Second Third-Party Plaintiff,

—against—

ANTHONY G. ANGELOS, et al.,

Second Third-Party Defendants.

Memorandum of Decision and Order
dated August 10, 1984

CV 82-1920

RAYMOND J. DONOVAN, Secretary of the United States Department of Labor,

Plaintiff,

—against—

JOHN CODY, et al.,

Defendants.

JOHN CODY, et al.,

Third-Party Plaintiffs,

—against—

ANTHONY G. ANGELOS, et al.,

Second Third-Party Defendants.

TEAMSTERS LOCAL 282 PENSION TRUST FUND,

Second Third-Party Plaintiff,

—against—

ANTHONY G. ANGELOS, et al.,

Second Third-Party Defendants.

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Memorandum of Decision and Order
dated August 10, 1984

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Memorandum of Decision and Order dated August 10, 1984

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Memorandum of Decision and Order dated August 10, 1984

MISHLER, District Judge

The court's memorandum of decision and order dated August 18, 1983 suggested that the venue for the third-party actions under 28 U.S.C. § 1404(a) should be the United States District Court for the Northern District of Illinois. Third-party defendant Jonathan D. Howe moved for change of venue to the United States District Court for the Northern District of Illinois. The court notes that the Fund (third-party plaintiff) instituted an action in the Northern District of Illinois based on substantially the same claims as is asserted here. The third-party defendants here are defendants in the Illinois action. Only the law firm of Jenner & Block are added defendants in the Illinois action.

Third-party Anthony G. Angelos moves to dismiss the complaint on various grounds pursuant to Rule 12(b) or for an order transferring venue to the Northern District of Illinois. Angelos' motion to dismiss is in all respects denied.

Howe's motion and Angelos' motion to transfer venue to the United States District Court for the Northern District of Illinois is granted.

SO ORDERED.

/s/ JACOB MISHLER
U.S.D.C.

Office-Supreme Court, U.S.
FILED
OCT 11 1984
ALEXANDER L. STEVAS,
CLERK

No. 84-352

IN THE

Supreme Court of the United States

OCTOBER TERM, 1984

JOHN CODY, ROBERT SASSO, JOHN DEE, WILLIAM ARGENTO, RALPH GUERCIA, HERBERT SCHNEIDER, and LOUIS NAPPI,

Petitioners,

vs.

RAYMOND J. DONOVAN, Secretary of the United States Department of Labor, and TED KATSAROS, JOHN KUEBLER, ROBERT TROTT, LAWRENCE KUDLA, and CHARLES CURD,

Respondents.

ON PETITION FOR WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE SECOND CIRCUIT

BRIEF IN OPPOSITION FOR RESPONDENTS TED KATSAROS, JOHN KUEBLER, ROBERT TROTT, LAWRENCE KUDLA, and CHARLES CURD.

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IN THE

SUPREME COURT OF THE UNITED STATES

October Term, 1984

Case No. 84-352

JOHN CODY, ROBERT SASSO, JOHN DEE, WILLIAM ARGENTO, RALPH GUERCIA, HERBERT SCHNEIDER, and LOUIS NAPPI,

Petitioners,

v.

RAYMOND J. DONOVAN, Secretary of the United States Department of Labor, and TED KATSAROS, JOHN KUEBLER, ROBERT TROTT, LAWRENCE KUDLA, and CHARLES CURD,

Respondents.

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE SECOND CIRCUIT

BRIEF IN OPPOSITION FOR RESPONDENTS TED KATSAROS, JOHN KUEBLER, ROBERT TROTT, LAWRENCE KUDLA AND CHARLES CURD

Opinions Below

The opinion of the United States District Court for the Eastern District of New York (Mishler, D.J.) severing the third-party claims, striking the jury demands, denying cross-motions for summary judgment, denying defendants' motions to dismiss under Rule 12(b)(7), and striking the punitive damages claim, filed April 5, 1983, is not reported, and appears in the Appendix to the Petition ("Appendix") at 30a. The District Court's opinion denying defendants' motion for recusal and application for certification under 28 U.S.C. § 1292(b), filed April 15, 1983, is not reported, and appears in the Appendix at 50a. The District Court's opinion following trial on the merits, filed July 21, 1983, is reported as Katsaros v. Cody, 568 F. Supp. 360 (E.D.N.Y. 1983), and appears in the Appendix at 57a. The District Court's opinion dismissing the third-party complaint of the Local 282

Pension Trust Fund ("Pension Fund") and dismissing all but the fraud claims of the Pension Fund Trustees, filed on August 18, 1983, is not reported, and appears in the Appendix at 81a. The District Court's opinion setting the damages and awarding attorneys fees, filed on December 7, 1983, is reported as Katsaros v. Cody, 4 E.B.C. 2613 (E.D.N.Y. 1983) and appears in the Appendix at 98a. The District Court's opinion settling attorneys fees, filed on January 26, 1984, is reported as Katsaros v. Cody, 4 E.B.C. 2698 (E.D.N.Y. 1984), and appears in the Appendix at 112a.

The opinion of the United States Court of Appeals for the Second Circuit (Lumbard, Mansfield and Kearse C.JJ.), filed June 29, 1984, is not yet reported, and appears in the Appendix at 3a. The order of the Court of Appeals denying rehearing, filed on July 26, 1984, appears in the Appendix at 1a.

Jurisdiction

The decision of the United States Court of Appeals for the Second Circuit was entered on June 29, 1984. (A. 3a). The jurisdiction of this Court over the Petition rests on 28 U.S.C. § 1254(1).

Questions Presented

The Petition asks the Court to review the following questions:

1. Whether the court of appeals contravened the Seventh Amendment to the United States Constitution and this Court's decision in Beacon Theatres, Inc. v. Westover, 359 U.S. 500 (1959), by affirming the district court's conduct of first severing "legal" third-party claims for which a jury trial had been demanded, from "equitable" main claims, and then conducting a bench trial of only the "equitable" claims without first trying the common factual issues between the "equitable" and "legal" claims before a jury.

The Court of Appeals, affirming the District Court, held that the District Court did not abuse its discretion in severing the third-party claims, since the main claims were ready for trial and the third-party claims were early in discovery; and held that the defendant Trustees were not entitled to a jury trial on the main claim since the plaintiffs sought only equitable relief. The District Court further held that the defendants had waived their right to a jury trial in Katsaros v. Cody.

2. Whether the unprecedented, excessive and unnecessarily punitive relief awarded by the district court, without ever hearing evidence relating to damages, and affirmed by the court of appeals, against the petitioner pension plan fiduciaries for making a single imprudent investment, including:(1) damages in the full amount of the loss ostensibly suffered by the pension

plan as a result of the imprudent investment, without considering any potential set-offs; (2) prejudgment interest at the above-prime rates that would have been realized by the imprudent investment; and (3) removal of the fiduciaries from their positions with not only the pension plan, but also its sister welfare, annuity and legal services trust funds, is justified under the Employee Retirement Income Security Act of 1974.

The Court of Appeals, affirming the District Court, found that the District Court did make provisions for potential set-offs against the amount to be paid by the Trustees in restitution (there was no award of damages to or against any party), and held that the District Court did not abuse its discretion in awarding prejudgment interest or removing the Trustees from their fiduciary positions. Petitioners did not raise the issue of "punitive

relief" in the Court of Appeals. Therefore, the question is not properly before this Court.

* * *

These questions are not worthy of certiorari; the decisions below are clearly correct, and there are no conflicts among the Circuits.

Statute Involved

This case involves the following provisions of the Employee Retirement Income Security Act of 1974 ("ERISA"). 29 U.S.C. Section 1104: set forth in the Petition, pp. 2 and 3; 29 U.S.C. Section 1105: set forth in the Petition, p. 3; 29 U.S.C. Section 1109: set forth in the Petition, pp. 3 and 4; 29 U.S.C. Section 1132(a):

> A civil action may be brought ... (3) by a participant, beneficiary, or fiduciary (a) to enjoin any act or practice which violates any term or provision of this title, or the terms of the plan, or (b) to obtain other appropriate equitable relief

(i) to redress such violation or (ii) to enforce any provision of this title ...

Statement of the Case

The Green Loan and Expenditures[1]

In February 1978, at a time when the Pension Fund's assets were valued at approximately $55,000,000, the Trustees (except Ralph Guercia, who was not yet a Trustee) approved a $35,000,000 loan to Hyman Green ("Green"). Green was to use $20,000,000 to purchase ten acres of land in Las Vegas and to build a gambling casino on the site. Green also agreed to purchase from the Pension Fund certain financially unproductive property in Southampton, New York for $15,000,000; however, the Pension Fund was to grant him a purchase money

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1. Petitioners make little reference to the Green loan in their Petition. In fact, this loan and the injunction issued against it by Judge Mishler played a major role in bringing about the removal of the petitioners from their positions.

mortgage for the full amount of the price. As part of the loan agreement, Green assumed responsibility for the Pension Fund's expenses in arranging the loan transaction.

In April 1978, the United States Secretary of Labor commenced an action entitled Marshall v. Teamsters Local 282 Pension Fund, 78 Civ. 543 ("Marshall action"), seeking to enjoin the Pension Fund and its Trustees from making the loan to Green. In August 1978, the District Court (Mishler, J.) issued a decision and order in the Marshall action finding that the proposed loan to Green violated Section 404(a)(1)(B) and (C) of ERISA, 29 U.S.C. § 1104(a)(1)(B) and (C). 458 F. Supp. 986 (E.D.N.Y. 1978).

The court found:

> "The proposed loan as outlined in the commitment issued by the trustees violates 29 U.S.C. §1104(a)(1)(B) and (C) in the following respects which present extra-ordinary risks:

(a) The project may not be completed for lack of equity capital.
(b) The project may not be completed because of strikes, increase in cost of construction, or poor management of construction.
(c) If completed, the hotel business may fail because of poor management, competition, or adverse economic conditions, or Las Vegas may lose its lure to gamblers because of competition in other parts of the country if gambling is legalized in states where it is now forbidden.
(d) If completed, the gambling casino may fail because of poor management or adverse economic conditions or competition.
(e) Government guaranteed Jennie May certificates are available bearing approximately the same interest rate as provided in the permanent mortgage.
(f) The Southampton land is saleable at a price in excess of cost, and it is imprudent and improper for the trustees to use a risky loan as a means of selling the Southampton property at a price in excess of market value for the purpose of showing increased total assets of the funds, knowing that the sale price is in excess of market value. It smacks of gimmickry.
(g) The loan represents a disproportionate commitment of the assets of the fund and violates 29 U.S.C. § 1104(a)(1)(B) and (C) and the trust agreement."

458 F. Supp. at 991.

The Pension Fund incurred $23,473.57 in expenses in arranging the loan to Green. Although Green had agreed to reimburse the Pension Fund for its expenses, he did not do so.

The Des Plaines Bancorporation Loan

On February 27, 1979, only six months after the preliminary injunction was issued in the Marshall action, the Trustees (now including Ralph Guercia) voted to loan $2,000,000 to the Des Plaines Bancorporation (hereinafter "Bancorporation"), a small bank holding company in a Chicago suburb.[2]

Prior to the Trustees' meeting of February 27, 1979, only one Trustee, John Cody ("Cody"), was even aware that

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2. There was little explanation at trial as to how it came about that a small Chicago bank came to a Long Island Teamster pension plan for a loan. Given the clear impropriety of the loan, this suspicious connection did not require further exploration.

Bancorporation would appear at the meeting with a loan request. All that Cody knew were the bare terms as stated in a letter. At the meeting, Anthony Angelos ("Angelos"), the principal of Bancorporation, and Jonathan Howe ("Howe"), a Bancorporation director, distributed Bancorporation's statements, as well as those of its subsidiary, the Des Plaines Bank (hereinafter the "Bank") to the Trustees. Angelos's personal financial statement was also distributed.

The Trustees devoted a half hour to examining the financial materials, during which time they were "walked through" the statements by Howe, who pointed out "improvements" in the Bank's condition. None of the Trustees had any background in accounting or in reading the financial statements. The Pension Fund accountant, though present, considered himself unqualified to interpret and analyze the financial statement, and did not express an opinion

as to the financial soundness of Bancorporation or Bank.

After some discussion and amendment of the terms of the loan, the Trustees unanimously approved the loan subject to an eyewitness examination of the Bank's premises and some of the real estate put up as collateral. After visiting the property on March 1, 1979, Cody and Guercia signed the various loan documents and had the funds disbursed. Less than 48 hours had passed since the Angelos and Howe presentation. No independent professional examination of Bancorporation's or the Bank's financial statements was done. The Bank's stock, taken as security, was not appraised or valued, nor was the real estate.

The loan was to be repaid within four years, with semiannual installments of $125,000 plus interest. At the end of four years, a balloon payment of $1,125,000

was due. Interest was to be calculated at prime plus 1% with a 10% floor. [3]

Only $500,000 of the loan proceeds was to be used to increase the capital of the Bank. The rest was paid to various creditors, including Angelos. One of the Bank's creditors, the Central National Bank of Chicago ("Central National"), was due to be repaid $1,000,000 on March 1, 1979. Prior to March 1979, Central National refused to extend its loan (for the third time) and threatened to foreclose and take over the Bank.

Had Trustees sought the assistance of a professional familiar with banking finances, they would have learned of serious deficiencies in the financial standing of Bancorporation and the Bank, all of which were indicated by the financial

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3. Given the prime rate at the time, the semiannual interest and principal payments should have been expected to exceed $250,000.

statements:

(a) Bancorporation had an extremely low and well below average earnings ratio of 3.4%.

(b) Bancorporation had an abnormally large "goodwill" allowance in the balance sheet; the deduction of the $1,300,000 listed as goodwill reduced its tangible net worth to only $500,000, about 25% of the loan being requested (before interest).

(c) The Bank showed an unusually rapid increase in loans between 1977 and 1978 (from $21.1 million to $32.7 million); normal growth would be 10% to 12%.

(d) The Bank, while increasing its loan portfolio, decreased its loan loss reserves to a ratio well below 1%, the norm for banks around the country in 1978.

(e) The ratio of Bank loans to deposits in 1978 was 67%, a high ratio.

(f) The net income of Bancorporation in 1978 was $278,000, while the amount of

annual payments to the Pension Fund for the loan would have exceeded $500,000 for the first year; neither the Bank nor Bancorporation ever earned that much money in any year in its history. [4]

The Trustees' omissions went beyond their failure to evaluate the financial statements or appraise the bank stock and real estate:

(a) They failed to obtain a title report on the real estate put up as security by Angelos. Had they done so, they would have found that prior liens totalling several hundred thousand dollars had been filed. They did not contact the predecessor lender, Central National, to ascertain

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4. It should be noted that Bancorporation was not the only bank holding company looking for capital in 1979. There was a market of several hundred such companies looking for loans, most of which were in better financial condition. The return offered by Bancorporation, 1% over prime, was generally available.

Bancorporation's repayment history or the reasons Central National had refused to extend further credit. They did not ask other Chicago-area financial institutions about the Bank's reputation in the financial community.[5] They did not meet with federal or state regulatory officials to obtain information about Bancorporation or the Bank.[6]

After the loan was disbursed, the Trustees did not receive the semiannual and annual financial data required and made no demand for it. When the statements began to reflect regulatory problems with the FDIC and Federal Reserve Board and

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5. In fact, five Chicago-area banks had refused to refinance the loan.

6. Officials of the FDIC had urged a ten-point corrective action plan for the Bank only six days before the February 27, 1979 Trustees' meeting. This plan dealt with undercapitalization, poor loan-to-deposit ratio, insufficient liquidity, substandard loans, and improper lending practices.

restrictions on Bank dividend payments (the principal source of funds for loan repayment), they took no action. Finally, the interest assessed to Bancorporation was miscalculated, resulting in a loss of over $32,000 to the Pension Fund.

On March 14, 1981, the Bank was closed by federal and state regulatory officials. At that time, the sum of $1,625,000 plus interest was due to the Pension Fund. No further payments were made.

Other Unlawful Activities

Prior to its determination on the appropriate relief, the Court was presented with evidence of additional improprieties by the Trustees:

(a) A $60,000 kickback to Cody and another Trustee by a real estate agent, following the purchase of a country club by the Pension Fund. See United States v. Cody, 722 F.2d 1052 (2d Cir. 1983).

(b) A $100,000 kickback to Cody by another real estate agent following another real estate purchase. Id.

(c) The payment of salaries to union business agents even though they were not performing services for the Pension Fund.

(d) Open and notorious evasion of payments to the Pension Fund by employers, including Trustee Guercia.

Relevant Procedural Background

The private Respondents commenced their action against the Trustees on July 14, 1981.[7] The answer filed by the Trustees on October 27, 1981 did not include a demand for a jury trial. (A. 35a). On December 20, 1982, the parties entered into a stipulation authorizing an amendment to the complaint in order to add the

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7. The later action filed by the Secretary of Labor was identical to that part of the private Respondents' action which sought relief with respect to the Bancorporation loan.

Pension Fund as a defendant. The amended complaint was filed on January 13, 1983. The only change involved the caption and a paragraph describing the Pension Fund. On January 24, 1983, the Trustees served an answer to the amended complaint, including a jury demand. The third-party complaint followed shortly thereafter. (Both the jury demand and the third-party complaint were filed more than one and a half years after commencement of the action.)

On plaintiffs' motion to strike the jury demand, the District Court held that the Trustees had waived their right to a jury trial and that that right had not been revived by the amended complaint. (A. 36a-38a). The District Court also held that the complaint was equitable in nature and did not require a jury trial. Finally, the Court held that the third-party fraud complaint did not include issues common with those in the main action, eliminating

any need for the ERISA action to be tried before a jury. (A. 40a-42a).

The District Court granted a motion to sever the third-party claims since (1) pretrial discovery had been completed in the main action while process was still being served in the third-party action, (2) none of the third-party defendants had even answered yet, and (3) delay would prejudice the plaintiffs. (A. 48a).

The trial was not bifurcated on the issue of liability and damages, although a separate proceeding was held, without objection by Trustees' counsel, on the form of relief. Contrary to their assertion (Petition p. 5), the Trustees were never denied an opportunity to introduce mitigating evidence. [8] One witness, called by the Pension Fund to testify about post-

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8. Judge Mishler, during trial, told counsel: "I will take what you give me, I will take whatever you offer."

default litigation, was not allowed to testify when plaintiffs stipulated that the Trustees had satisfactorily pursued post-default remedies.

The District Court found that the Trustees breached their fiduciary obligations by relying solely on the information and representations given by the borrowers and failing to conduct an independent investigation. (A. 71a).

Prior to determining the remedy and entering judgment, the Court received affidavits from plaintiff Lawrence Kudla and from counsel to the Trustees. Since there seemed to be no factual disputes, an evidentiary hearing was unnecessary.

Each of these actions by the District Court was affirmed by the Court of Appeals.

REASONS FOR DENYING A WRIT

I

The severance of Petitioners' third-party claims from Respondents' equitable claims was neither an abuse of discretion nor a violation of Petitioners' right to a trial by jury.

A. The Trustees Waived Their Right To A Jury Trial.

To bring themselves under this Court's rule in Beacon Theatres, Inc. v. Westover, 359 U.S. 500 (1959), Petitioners must first have properly demanded a jury trial. They neglect to tell the Court that they did not.

In answering the complaint in September 1981, the Trustees did not demand a jury trial. Their first such demand was made in their January 1983 answer to the amended complaint. No motion was ever made for leave to file such a demand. The issue was addressed by the District Court on a motion to strike the demand.

Rule 38(b) of the Federal Rules of Civil Procedure requires that a demand for

a jury trial be served within ten days after service of the "last pleading directed to such issue." If a demand is not filed, it is waived. The amendment of a complaint does not revive the right, if waived, to demand a trial on issues fairly raised in the original pleadings. State Mutual Life v. Arthur Andersen & Co., 581 F.2d 1045, 1049 (2d Cir. 1978); Walton v. Eaton, 563 F.2d 66 (3d Cir. 1977); Moore v. U.S., 196 F.2d 906 (5th Cir. 1952); Olund v. Swarthout, 459 F.2d 999 (6th Cir. 1972), cert. denied, 409 U.S. 1008 (1973); Trixler Brokerage Co. v. Ralston Purina Co., 505 F.2d 1045 (9th Cir. 1974); Ward v. Brown, 301 F.2d 445 (10th Cir. 1962); Railex Corp. v. Joseph Guss & Sons, Inc., 40 F.R.D. 119 (D.D.C. 1966), affirmed, 382 F.2d 179, 127 U.S. App. D.C. 230 (1967).

In the instant action no new issues were added by the First Amended Complaint -- its purpose was to add a new party, the

Pension Fund, which the Trustees asserted was an indispensable party. The Trustees offered no justification for the year and a half delay and were properly denied a jury trial.

B. Even If Petitioners Had Not Waived A Jury Trial They Were Not Entitled To One.

1. The Severance Of The Main Action From The Third-Party Action Was Proper.

The private respondents commenced their action in July 1981. Third-party complaints were not filed in their case until January 1983, eighteen months later. At the time of the ruling (less than three weeks before trial), the parties in the main action had completed all discovery and were ready for trial. At the same time, Petitioners had not even served all of the third-party defendants. The four who were served had not answered and were challenging the court's in personam jurisdiction. Discovery had not yet

commenced and trial was at least a year off. [9] The discovery and trial of the third-party claims involved complex issues having no relevance to the issues in the main action. Continued joinder promised to invite confusion and delay, a clear frustration of efficient justice.

Delay of the trial would have long postponed the remedy sought by the plaintiffs: removal of the Trustees. Every day they remained in office compounded the potential harm to the Pension Fund participants. Given the persistent nature of their misconduct, additional delays in the proceedings threatened the integrity of the Pension Fund.

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9. In fact, at this date, one and one half years later, the action is still in a preliminary stage.

2. The Claims In The Main Action Were Purely Equitable In Nature.

It is well established that actions seeking restitution for a breach of fiduciary duty are equitable in nature. S.E.C. v. Commonwealth Chemical Sec., 574 F.2d 90, 95 (2d Cir. 1978). ERISA Section 409(a), 29 U.S.C. § 1109(a), the statute governing this action, explicitly refers to "equitable and remedial relief." The Seventh Amendment right of jury trial does not attach to matters lying within the Court's equity jurisdiction. Katchen v. Landy, 382 U.S. 323, 337 (1966). Accordingly, there is no right to a jury trial of ERISA actions against trustees seeking the equitable remedy of restitution.[10] See also In re Vorpahl, 695 F.2d 318, 320-22 (8th Cir. 1982); Calamia v. Spivey, 632 F.2d 318, 320-22 (5th Cir. 1980); Wardle v. Central

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10. Petitioners do not challenge the holding of the Court of Appeals in this respect.

States, Southeast & Southeast Areas Pension Fund, 627 F.2d 820, 829-30 (7th Cir. 1980), cert. denied, 449 U.S. 1112 (1981).

3. The Severance Of The Third-Party Action Did Not Deny Petitioners Their Right To A Jury Trial.

Petitioners argue that there were factual issues common to the main action and the third-party complaints. This, they assert, required that the main action be tried before a jury because of a potential denial of their Seventh Amendment rights through the later application of the doctrine of collateral estoppel.

The District Court found that the issues in the main action against the Trustees were not the same as the issues in the third-party actions. (A. 48a). The issue of fraudulent disclosure raised by the Trustees in the third-party action was deemed "separate," "unrelated," and of "doubtful relevancy" to the question of the Trustees' prudence -- the subject

matter of the main claim.[11] The core facts involved in the trial concerned the actions taken by the Trustees to investigate, review and evaluate Bancorporation's loan proposal other than their conversations with the Bancorporation directors. Given the lack of relationship between the issues in the main case and the third-party complaint, the District Court was not wrong in denying a jury trial on the severed equitable portion of the case.

To the extent that issues may later arise in the third-party action which may invite the application of collateral estoppel, this Court's decision in Parklane Hosiery Co. v. Shore, 439 U.S. 322 (1979) clearly governs. The Court recognized in Parklane that its holdings in Beacon Theatres v. Westover, 359 U.S. 500 (1959),

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11. At trial, the Trustees did not even raise the allegation that they had been defrauded as a defense to the allegations of the complaint.

"enunciated no more than a general prudential rule," Id. at 334, and that

> "'... there might be situations in which the Court could proceed to resolve the equitable claim first even though the results might be dispositive of the issues involved in the legal claim.'"

439 U.S. at 335, citing Katchen v. Landy, supra at 339.

In Parklane Hosiery, this Court held that an equitable determination can have collateral estoppel effect in a subsequent legal action and that this estoppel does not violate the Seventh Amendment. See also Crowder v. Lash, 687 F.2d 996, 1009-1011 (7th Cir. 1982); Consolidated Express Inc. v. N.Y. Shipping Assn., Inc., 602 F.2d 491 (3d Cir. 1979), vacated on other grounds, 448 U.S. 902 (1980).

The Court thus distinguished Beacon Theatres, which involved a counterclaim. The third-party complaint in the instant action has more in common with the subsequent action addressed in Parklane Hosiery

than the counterclaim in Beacon Theatres. The third-party complaint was brought one and a half years after the main action commenced and was in the most preliminary of stages when the trial of the main action was held. At the time of trial, answers had not been interposed and affirmative defenses concerning justifiable reliance had not yet been raised by the third-party defendants.

These facts, combined with the District Court's finding that the tactic of bringing a third-party complaint was employed for the "purpose of delay and employed in bad faith" (A. 107a), weigh heavily against utilization of this case as a vehicle to consider the expansion of the prudential rule of Beacon Theatres.

II

The relief granted by the District Court and affirmed by the Court of Appeals was well within its discretion and was permitted by ERISA.

Despite their repeated violations of the fiduciary provisions of ERISA, and the fact that the Bancorporation default deprived the Pension Fund of other opportunities to gain a high rate of return on an investment, the Trustees complain that the District Court was unjustified in removing them from office and assessing prejudgment interest in an amount equal to that which the Pension Fund would have received had Bancorporation not defaulted. Given the nature and extent of the Trustees' violations and the courts' broad equitable powers under ERISA, the Trustees are surely mistaken.

The remedial provisions of ERISA give the courts broad powers over fiduciaries and employee benefit plans in the shaping

of remedial relief. Section 502(a) of ERISA, 29 U.S.C. § 1132(a), provides:

> "A civil action may be brought ... (3) by a participant, beneficiary, or fiduciary (a) to enjoin any act or practice which violates any term or provision of this title or the terms of the plan, or (b) to obtain other appropriate equitable relief (i) to redress such violation or (ii) to enforce any provision of this title ..." (emphasis added).

Section 409 of ERISA, 29 U.S.C. § 1109, provides:

> "Any person who is a fiduciary with respect to a plan who breaches any of the responsibilities, obligations, or duties imposed upon fiduciaries by this subchapter shall be personally liable to make good to such plan any losses to the plan resulting from each such breach, and to restore to such plan any profits of such fiduciary, and shall be subject to such other equitable or remedial relief that the court may deem appropriate, including removal of such fiduciary ...." (emphasis added).

The reports of the various committees concerning Section 409 of ERISA make it clear that Congress intended to provide the courts with broad remedies for

redressing the interests of participants and beneficiaries when they have been adversely affected by breaches of fiduciary duty.

> "The enforcement provisions have been designed specifically to provide both the Secretary and participants and beneficiaries with broad remedies for redressing or preventing violations of the Retirement Income Security for Employees Act .... The intent of the committee is to provide the full range of legal and equitable remedies available in both state and federal courts ..."

S. Rep. No. 83-127, 93rd Cong., 1st Sess., Reprinted [1974], U.S. Code Cong. & Admin. News, pp. 4838, 4871. Also, see generally Marshall v. Snyder, 572 F.2d 894, 901 (2d Cir. 1978); Eaves v. Penn, 587 F.2d 453, 462 (10th Cir. 1978); Iron Workers Local No. 272 v. Bowen, 624 F.2d 1255, 1262 (5th Cir. 1980); Marshall v. Kelly, 465 F. Supp. 341, 354 (W.D. Okla. 1978).

In developing a law of remedies, Congress intended the federal courts to

draw upon the principles of traditional trust law:

> "The objectives of these provisions are to make applicable the law of trusts; ... and to establish uniform fiduciary standards to prevent transactions which dissipate or endanger plan assets; and to provide effective remedies for breaches of trust."

Statement of the Honorable Harrison A. Williams, Jr., 120 Cong. Rec. S-15737, August 22, 1974, Reprinted [1974], U.S. Code Cong. & Admin. News, pp. 5177, 5186.

Traditional trust law provides for broad and flexible equitable remedies in cases involving violations of fiduciary duty. Generally, the court has a duty to fashion the remedy which is most advantageous to the participants and most conducive to effectuating the purposes of the trust. Eaves v. Penn, supra.

The use of the words "other appropriate equitable relief" illustrates

Congress's intention to allow the courts great flexibility in fashioning such relief. This Court, in Hall v. Cole, 412 U.S. 1 (1974), interpreted the breadth of relief available under Section 102 of the Labor-Management Reporting and Disclosure Act of 1959, 29 U.S.C. § 412, which similarly authorizes the courts to grant "such relief . . . as may be appropriate." These words were construed as a "broad mandate to the courts." The Court further stated that any attempt by Congress "to spell out all of the remedies available under § 102 would create the 'danger that those remedies not listed might be proscribed with the result that the courts would be fettered in their efforts to grant relief according to the necessities of the case.'" Id. at 11. The Trustees would have this Court engage in such limitations. The Court should decline to do so.

A. Removal Of The Trustees For Repeated Egregious Violations Of The ERISA Fiduciary Standards Was Warranted.

There is no conflict in the Circuits as to whether the removal of fiduciaries from their positions with employee benefit plans governed by ERISA is appropriate where they have engaged in "repeated or substantial violation[s] of [their] responsibilities," or "threatened dissipation of [plan] assets." Marshall v. Snyder, 572 F.2d 894, 901. Iron Workers Local No. 272 v. Bowen, supra. See also S. Rep. No. 383, 93 Cong., 2d Sess., reprinted in 1974, U.S. Code Cong. & Admin. News 4890, 4989 (set out in the opinion of the Court of Appeals at A. 23a).

The breaches of trust committed by Petitioners were not, as they would have this Court believe, two isolated incidents of imprudence involving "mere error[s] in their business judgment." (Petition, p. 16). The violations of law were flagrant

and involved great risk to the Pension Plan funds. The commitment of 65% of the Pension Fund assets to a risky loan involving the construction of a Las Vegas casino, the disbursement of $2,000,000 on 48 hours notice to an unknown and uninvestigated suburban Chicago bank on the verge of failure, the receipt of $160,000 in kickbacks by the Pension Fund manager and Trustee, and unlawful payments to union business agents, and the unlawful expenditure of Pension Fund assets to defend these unlawful activities, amounts to a pattern of persistent, reckless, and lawless conduct which could only be properly remedied by removal from office. The District Court's action was remedial, not punitive. As such, it was a proper exercise of the court's discretion.

B. The Calculation Of Prejudgment Interest Was A Proper Exercise Of The District Court's Discretion.

The District Court's assessment of prejudgment interest at the rate provided for in the Bancorporation loan was a proper exercise of its discretion.

ERISA grants the Court wide discretion to shape the relief necessary to make a pension fund whole. Gilliam v. Edwards, 492 F. Supp. 1255, 1266-1267 (D.N.J. 1980). This includes the assessment of interest against a trustee found liable for wrongful disposition of trust funds from the time of loss. Id. The determination of the appropriate rate of interest to compensate the beneficiaries for the Trustees' breach of duty is committed to the Court's discretion. Donovan v. Bryans, 566 F. Supp. 1258, 1265 (E.D. Pa. 1983).

Petitioners suggest that the rate of interest to be assessed should correspond to the Pension Fund's average annual rate

of return -- 8% to 9%. This figure, however, does not reflect an accurate annual rate of return on money newly invested during the period between the loan default and the entry of judgment. The Pension Fund's average annual rate of return was (and remains) handicapped as a result of longstanding but low-yielding investments in the Pension Fund's portfolio, including previously purchased low-yielding corporate bonds.

For the Court's remedy to be appropriate, the rate of interest to be assessed must reflect a return on newly invested funds during 1980-1983 as opposed to the rate of return on sluggish investments made previous to the period in question.

Expert testimony at trial revealed that at the time the Bancorporation loan was made, "several hundred" other banking institutions were in the market to borrow at a probable rate of 1% above prime. The

terms of the Bancorporation loan were not unusual given the high interest rates in effect for all borrowers during the 1979-1983 period.

Had the money been invested prudently, the participants and beneficiaries of the Pension Fund would have reaped the benefit of the then prevailing high interest rates. As a result of Petitioners' imprudence and mismanagement, the participants and beneficiaries were denied that opportunity. In order to make the Pension Fund whole, the benefit that was to be gained from the now lost opportunity had to be restored. This is what the District Court did.[12]

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12. The assertion by Petitioners that their conduct was not egregious and that the losses to the Pension Fund occurred despite their good faith efforts is belied by the facts, as reviewed above, and the reckless manner in which they committed the Pension Fund to the Bancorporation loan.

C. The District Court Did Make Proper Provision For Set-Offs.

In its opinion concerning the form of relief, the District Court stated:

> "Payments received by the Fund on account of the loan will be credited against the judgment sum."

There was no requirement, in law or equity, that the District Court refrain from entering judgment until the Trustees completed their various efforts to collect against the loan collateral and in their common law fraud actions against the Bancorporation directors. Whatever money the Petitioners recover will be set off against the judgment sum.

As one court noted, when considering a similar factual situation:

> "The possibility that either the Plan or participants might be made whole through other proceedings ... does not require the Court to withhold the remedy provided in these proceedings. The defendants are in no danger of multiple judgments, and equity can resolve any contribution or indemnity to which

> they may become entitled by virtue of making good the loss to the Plan."

Freund v. Marshall and Ilsley Bank, 485 F. Supp. 629, 643 (W.D. Wis. 1979).

D. The Relief Granted Was Appropriate And Was Not Punitive.

In addition to arguing that each form of relief granted by the District Court was unwarranted, Petitioners, for the first time, argue that the relief amounted to punitive damages and should be vacated as contrary to ERISA. That issue was not raised in the Court of Appeals and therefore is not properly before this Court. Ramsey v. United Mine Workers, 401 U.S. 302, 312 (1971).

In fact, the District Court itself struck plaintiffs' demand for punitive damages. (A. 47a). The relief granted -- removal of the Trustees from office, restitution and the assessment of interest -- was remedial in nature and was well

within the equitable powers of the District Court.

* * *

The questions raised by the District Court's grant of relief, as affirmed by the Court of Appeals, are hardly appropriate for this Court's consideration.

Conclusion

For the foregoing reasons, the petition for certiorari should be denied.

Dated: New York, New York
October 9, 1984

Respectfully submitted,

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FILED
NOV 9 1984

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No. 84-352

In the Supreme Court of the United States

OCTOBER TERM, 1984

JOHN CODY, ET AL., PETITIONERS

v.

RAYMOND J. DONOVAN, SECRETARY OF LABOR, ET AL.

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE SECOND CIRCUIT

BRIEF FOR THE FEDERAL RESPONDENT IN OPPOSITION

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14 pp

QUESTIONS PRESENTED

1. Whether the district court abused its discretion in severing petitioners' third-party claims for separate trial.

2. Whether the district court abused its discretion in granting relief for a breach of fiduciary duties imposed by the Employee Retirement Income Security Act of 1974.

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ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE SECOND CIRCUIT

BRIEF FOR THE FEDERAL RESPONDENT IN OPPOSITION

OPINIONS BELOW

The opinion of the court of appeals (Pet. App. 3a-27a) is reported at 744 F.2d 270. The district court's memorandum of July 21, 1983 (Pet. App. 57a-80a) is reported at 568 F. Supp. 360. The district court's memorandum of December 7, 1983 (Pet. App. 98a-107a) is reported at 4 Empl. Ben. Cas. (BNA) 2613. The district court's memorandum of January 26, 1984 (Pet. App. 112a-119a) is reported at 4 Empl. Ben. Cas. (BNA) 2698. The district court's memoranda of April 5, 1983 (Pet. App. 30a-49a), April 15, 1983 (*id.* at 50a-56a), August 18, 1983 (*id.* at 81a-97a), and August 10, 1984 (*id.* at 133a-137a) are unreported.

JURISDICTION

The judgment of the court of appeals was entered on June 29, 1984. A petition for rehearing was denied on July 26, 1984 (Pet. App. 1a-2a). The petition for a writ of certiorari

was filed on September 4, 1984. The jurisdiction of this Court is invoked under 28 U.S.C. 1254(1).

STATEMENT

1. Petitioners were trustees of the Teamsters Local 282 Pension Trust Fund and Welfare, Annuity and Legal Services Trust Funds. Separate actions against petitioners by participants in the Pension Fund and by the Secretary of Labor were consolidated in the United States District Court for the Eastern District of New York. Following a bench trial, petitioners were removed from their positions and held jointly and severally liable to the Pension Fund for losses resulting from breaches of their fiduciary duties under the Employee Retirement Income Security Act of 1974 (ERISA), 29 U.S.C. 1001 *et seq.* (Pet. App. 57a-80a, 98a-107a). With the exception of a provision of the district court's order relating to appointment of a fund manager, the court of appeals affirmed (*id.* at 3a-27a).

a. The evidence at trial showed that petitioners approved a $2 million loan from the Pension Fund to Des Plaines Bancorporation for its wholly owned subsidiary, the Des Plaines Bank. Representatives of Bancorporation made a two-hour presentation to petitioners on February 27, 1979, discussing the highlights of certain of their financial statements. Although petitioners possessed neither accounting nor banking expertise, they did not obtain independent professional analysis of the data. Following further discussions with two of the trustees, loan documents were signed on March 1, 1979. The loan agreement provided for repayment in semi-annual installments of $125,000 plus interest, with a final balloon payment after four years of $1.125 million. Interest was payable at 1% over the prime rate. Security for the loan was 95% of the Bank's outstanding stock as well as certain property owned in part by Bancorporation's president. Pet. App. 9a-11a.

The Pension Fund received three of the required payments. On March 14, 1981, the Bank was closed by federal and state regulatory officials, and no further payments were made. At that time, Bancorporation owed the Pension Fund $1.625 million, plus interest from September 1980. Pet. App. 11a.

b. The courts below concluded that petitioners breached their fiduciary duties under ERISA's prudent-man standard in connection with the loan.[1] As summarized by the court of appeals (Pet. App. 19a):

> The trustees, being ill-equipped to evaluate the soundness of the proposed loan, failed to observe their duty to seek outside assistance. They relied exclusively on the representations of Bancorporation, the borrower, as to its financial strength and reached an investment decision after wholly inadequate inquiry and deliberation. A reasonable investigation would have revealed evidence that the loan was totally unsound.

Among the "red flags" (*id.* at 12a) that an appropriate inquiry would have uncovered were the Bank's extremely low equity/asset ratio, its tangible net worth of one-quarter the amount of the loan, an abnormal rise in the amount of its loans, its difficulty in meeting payments on another loan and in obtaining funds elsewhere, and criticism of the Bank's operations by officials of the Federal Deposit Insurance Corporation shortly before Bancorporation's meeting with petitioners (*id.* at 12a-13a, 71a-76a).

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[1] 29 U.S.C. 1104(a)(1) provides:

> [A] fiduciary shall discharge his duties with respect to a plan solely in the interest of the participants and beneficiaries and —
>
> * * * * *
>
> (B) with the care, skill, prudence, and diligence under the circumstances then prevailing that a prudent man acting in a like capacity and familiar with such matters would use in the conduct of an enterprise of a like character and with like aims * * *.

c. Following a hearing on relief, the district court held petitioners liable to the Pension Fund for $2.5 million to compensate for the Fund's loss in connection with the Bancorporation loan (Pet. App. 101a).[2] The court also removed petitioners from their positions as trustees of the various Funds (*id.* at 104a-107a, 122a). The court of appeals affirmed the relief, except with respect to the term of a fund manager appointed by the district court (*id.* at 22a-27a).

2. Following commencement of the actions against them, petitioners filed third-party claims against Bancorporation's directors and counsel, alleging common-law fraud and misrepresentation in connection with the loan.[3] In a pretrial order, the district court severed the third-party claims pursuant to Fed. R. Civ. P. 42(b) because they were still at a preliminary stage and a delay in trying the main actions would "substantially prejudice the rights of the plaintiffs" (Pet. App. 48a). The court rejected petitioners' argument that all of the actions must be tried together to a jury in order to preserve their jury-trial right with respect to

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[2]This amount included $1.625 million in unpaid principal, $700,000 in unpaid interest as provided in the loan agreement, $142,000 in interest at the prime rate for the nine months from the date of maturity of the loan to judgment, and $32,000 in prior uncollected interest. The court also held petitioners (except for Guercia, who was not a trustee at the relevant time) liable for $23,000 in connection with an unrelated transaction. Pet. App. 101a.

[3]Petitioners also alleged violations of the securities laws; these were dismissed for failure to state a claim (Pet. App. 90a, 97a). The Pension Fund, which had been joined as a defendant in the main actions, brought third-party claims seeking indemnification from the Bancorporation officials. These were dismissed as "inaccurately based upon notions of derivative liability" (*id.* at 89a-90a, 97a). The Fund subsequently filed an independent action against the officials in the United States District Court for the Northern District of Illinois. That case was dismissed on grounds of collateral estoppel arising out of the main actions (*id.* at 125a-132a; 585 F. Supp. 1401, appeal docketed, No. 84-2141 (7th Cir. July 11, 1984)).

the third-party claims under *Beacon Theatres, Inc.* v. *Westover*, 359 U.S. 500 (1959). The court reasoned that "[t]he issues in the actions against [petitioners] are not the same as the issues in the third-party actions" (Pet. App. 40a) and so collateral estoppel would not foreclose petitioners' access to a jury on their claims against the Bancorporation officials (*id.* at 39a-42a). The district court subsequently transferred the third-party claims to the United States District Court for the Northern District of Illinois, where they are currently pending (*id.* at 133a-137a).

ARGUMENT

Petitioners contend that the actions against them and their third-party action raised common issues requiring resolution by a jury and that the relief granted by the district court was excessive. These largely factbound claims were correctly rejected by the courts below. Further review is unwarranted.

1. Petitioners contend (Pet. 9-14) that severance of their third-party claims for later trial was improper under *Beacon Theatres*.[4] There, the Court held that where legal claims and equitable claims in the same action raise identical issues of material fact, the legal claims normally should be tried first. 359 U.S. at 510-511. This rule is designed to preserve the right to a jury determination of the legal claims in view of the possibility that later litigation before a jury might be precluded by the court's determination of the facts in connection with the equitable claims. See *Parklane Hosiery Co.* v. *Shore*, 439 U.S. 322, 333-334 (1979).

This principle is inapplicable here, because the issues decided in the main actions are for the most part irrelevant to the third-party claims. The basic question in the main

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[4]Petitioners do not press their claim, rejected by the courts below (Pet. App. 17a-18a, 34a-39a), that they were independently entitled to a jury trial of the claims against them.

actions was whether the trustees conducted themselves as prudent persons within the meaning of 29 U.S.C. 1104(a)(1)(B) (note 1, *supra*) in deciding to make the loan to Bancorporation. This issue is wholly irrelevant to petitioners' fraud claims, as they appear to admit (Pet. 12 n.8). See Restatement (Second) of Torts §§ 540, 545A (1977) (recipient of fraudulent information is justified in relying on it even if its falsity might have been ascertained by investigation; action is not barred by the recipient's contributory negligence). And while contributory negligence may bar recovery for negligent misrepresentation (*id.* § 552A), whether petitioners would be barred under this doctrine was not actually decided in the main actions. Rather, the district court found simply that petitioners failed to meet the high standard of care imposed by ERISA upon trustees (Pet. App. 69a-70a). Petitioners remain free to argue that they did satisfy the standard of care required of them to recover for common-law misrepresentation.[5] Accordingly, collateral estoppel should not operate to deprive petitioners of a jury trial on their third-party claims.[6]

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[5]See generally Restatement (Second) of Trusts § 227 comment e (1959) ("[i]n making investments not only is the trustee under a duty to use due care and skill, but he must use the caution of a prudent man"); G. Bogert, *The Law of Trusts and Trustees* § 541, at 167 (rev. 2d ed. 1978) (discussing higher standard of care for professional trustees); *Donovan* v. *Mazzola*, 716 F.2d 1226, 1231 (9th Cir. 1983), cert. denied, No. 83-598 (Jan. 9, 1984) ("in enacting ERISA Congress made more exacting the requirements of the common law of trusts relating to employee benefit trust funds"); *Donovan* v. *Bierwirth*, 680 F.2d 263, 272 n.8 (2d Cir.), cert. denied, 459 U.S. 1069 (1982) (duties of trustees under ERISA are "the highest known to the law").

[6]The decision foreclosing litigation by the Pension Fund (see note 3, *supra*) is, we submit, based on an incomplete analysis of the issues; the court focused primarily on whether the Fund participated in the earlier litigation sufficiently to be estopped (see Pet. App. 129a-132a). In any event, it would make little sense to vacate an otherwise valid judgment and remand for a new trial simply because a different court in a distinct

Even if collateral estoppel might arise, the decision of the district court severing the third-party claims for later trial was nonetheless correct. The need to prevent irreparable harm to the Pension Fund's participants arising from its direction by trustees who had violated the trust reposed in them dictated a trial at the earliest possible time.[7] Moreover, the actions against petitioners were ready for trial while "the third party claims were still early in discovery; indeed, not all of the third parties had been served, much less deposed or subjected to discovery requests" (Pet. App. 16a). Under these circumstances, the "general prudential rule" (*Parklane Hosiery*, 439 U.S. at 334) of *Beacon Theatres* must give way, as the Court recognized in *Beacon Theatres* itself (359 U.S. at 510). See *Katchen* v. *Landy*, 382 U.S. 323, 339-340 (1966) ("[b]oth *Beacon Theatres* and *Dairy Queen* [v. *Wood*, 369 U.S. 469 (1962),] recognized that there might be situations in which the Court could proceed to resolve the equitable claim first even though the results might be dispositive of the issues involved in the legal claim").

2. Petitioners contend (Pet. 14-23) that the relief ordered by the district court was excessive. It is, however, "well-settled that ERISA grants the court wide discretion in fashioning equitable relief to protect the rights of pension

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action disagrees with the first court's reasonable prediction concerning the scope of its own judgment. We note that the problem arose here solely because of the transfer of the legal claims to another court, a situation unlikely to arise with great frequency.

[7]Most of the petitioners had committed other serious violations of ERISA in the past. See *Marshall* v. *Teamsters Local 282 Pension Trust Fund*, 458 F. Supp. 986 (E.D.N.Y. 1978). Indeed, petitioner Cody, who by virtue of his economic power over the other trustees possessed complete control over the Pension Fund, had been convicted under the Racketeer Influenced and Corrupt Organizations Act (18 U.S.C. 1961 *et seq.*) in connection with his receipt of kickbacks as a fiduciary of the Pension Fund. Pet. App. 102a-103a.

fund beneficiaries" (Pet. App. 22a).[8] See, *e.g.*, *Donovan* v. *Mazzola*, 716 F.2d 1226, 1235 (9th Cir. 1983), cert. denied, No. 83-598 (Jan. 9, 1984); *Eaves* v. *Penn*, 587 F.2d 453, 462 (10th Cir. 1978). In view of petitioners' misconduct, the relief awarded was well within this discretion. Petitioners' argument that the courts below erred in applying settled law to the facts of this case does not warrant this Court's review.

Removal of petitioners from their positions, a remedy expressly authorized by 29 U.S.C. 1109 (note 8, *supra*), was wholly proper in light of the violations found by the courts below. See Pet. App. 23a-24a; *Mazzola*, 716 F.2d at 1238-1239; *Marshall* v. *Snyder*, 572 F.2d 894, 901 (2d Cir. 1978). Petitioners' attempt to reargue the facts (Pet. 15-18) by suggesting that only a "mere error of judgment" was involved must fail (see pages 2-3, *supra*). The award of prejudgment interest was proper in view of the fact that hundreds of other banks were willing to borrow funds at the same rate (Pet. App. 22a-23a). Accordingly, the award of interest merely put the Fund in the position it would have occupied but for petitioners' improvident loan to Bancorporation. See 29 U.S.C. 1109; *Mazzola*, 716 F.2d at 1232-1233, 1235; Restatement (Second) of Trusts § 205 &

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[8] 29 U.S.C. 1109(a) provides:

> Any person who is a fiduciary with respect to a plan who breaches any of the responsibilities, obligations, or duties imposed upon fiduciaries by this subchapter shall be personally liable to make good to such plan any losses to the plan resulting from each such breach, and to restore to such plan any profits of such fiduciary which have been made through use of assets of the plan by the fiduciary, and shall be subject to such other equitable or remedial relief as the court may deem appropriate, including removal of such fiduciary. * * *

comment a (1959).[9] Finally, contrary to petitioners' unsupported contention (Pet. 22), there is no requirement that all set-offs be incorporated into a single judgment. Cf. Fed. R. Civ. P. 13(i). Credits in favor of petitioners reflecting recovered funds will amply protect their interests.

CONCLUSION

The petition for a writ of certiorari should be denied.

Respectfully submitted.

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NOVEMBER 1984

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[9] In the *Bierwirth* case, relied upon by petitioners (Pet. 20-21), the court ultimately determined that the pension fund there had not suffered any loss; accordingly, no issue of prejudgment interest was presented. See 5 Empl. Ben. Cas. (BNA) 1065 (E.D.N.Y. Feb. 21, 1984), appeal pending, No. 84-6130 (2d Cir.). In any event, there is no requirement that the courts' equitable discretion be exercised in an identical fashion in every case.

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